

Nonproperty Taxation for Schools

Possibilities for Local Application

ALBERT L. ALFORD, *Specialist*
Public Finance and School Support

U.S. DEPARTMENT OF
HEALTH, EDUCATION, AND WELFARE

Anthony J. Celebrezze
Secretary

Office of Education
Francis Keppel, Commissioner

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FOREWORD

A GROWING interest in the use of nonproperty sources to replace an overburdened property tax, actually or psychologically, has been evident in recent years, particularly as school district levies have been running into stiff voter opposition. However, because school districts have relied on the property tax for their major and often sole source of local taxes for so long, there has been little development of information relative to nonproperty taxes for schools. The major emphasis for seeking relief has been in increased State aid programs.

The purpose of this study is to present some broad information on the possibilities of local nonproperty tax adoption and to bring together in a resource document as much information as possible on local nonproperty taxes and related problems.

It is hoped that the discussion of the various nonproperty taxes will be useful to persons considering the application of such sources to their school district. Although such adaptations are always in the final analysis subject to considerable local modification, broad guidelines and source information can be useful. Perhaps more than in most public policy decisions, emotional and special economic considerations play an important part in molding tax programs. However, a number of views and facts can be useful in the development of a sound tax program, and it is to that purpose that this study is dedicated.

Many persons in various parts of the country over the 2-year period involved in the assembly and preparation of material have contributed to this study, directly or indirectly. Though they are too numerous to mention by name, sincere thanks are extended to the officials and staff members of State education departments, education associations, tax commissions or departments, budget offices, legislative advisory staffs, and taxpayers associations; local school superintendents and their staffs; local budget and tax personnel; and the many others who have been consulted.

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FRED F. BEACH, *Director*
Administration of State
and Local School Systems

ERIC R. BABER
Assistant Commissioner
Division of Elementary and
Secondary Education

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CHAPTER 1

Evolution of the Property Tax

PROPERTY TAXES play such an important role in school finance and relate so directly to the problem of local nonproperty taxes that it is important to review the status of the property tax and these relationships before proceeding to a consideration of the main subject of this study.

Mainstay of School District Local Financing

Taxation of property—real, personal, tangible, and intangible—is still the mainstay of school district local financing and plays a significant role in providing revenue for other local government services. In fiscal year 1960, over 87 percent of locally raised taxes came from the property tax. In the category of general revenue from own sources, i.e., locally raised revenue, the property tax provided almost 69 percent of the total; and in total general revenue, the property tax comprised 48 percent. General revenue includes all revenue except that resulting from utility, liquor store, or insurance trust operations.

For financially independent school districts, the property tax plays an even more important role. In 1957, the property tax comprised almost 99 percent of all taxes collected and almost 86 percent of all revenue from own sources. The property tax made up approximately 50 percent of all revenue received by independent school districts. State aid made up almost all the remainder.

In this study, the Bureau of the Census classifications of "independent" and "dependent" school systems will be followed. Those systems which are administratively and fiscally independent of any other government are classified as independent. If some element in this autonomy is missing, then the school systems are considered as dependent activities of the unit of government which has a legal element of control—a county, municipality, town, township, or State government. Most commonly the element of control involves authority to determine the level of expendi-

tures. Even if this authority is unused in practice, the school system will be classified as dependent so long as the legal limitation remains.¹

Dependent school districts enroll approximately 22 percent of public school pupils, and in these districts, the property tax plays a slightly less important role, ranging from the high percentages noted for the independent school districts down to about 67 percent of all local taxes collected in New York City. The other categories, revenue from own sources and total revenue, carry correspondingly lower figures. In general terms, the property tax represents a critical factor even in financially dependent districts because most large cities and counties rely on it for a higher percentage of revenue than does New York City (34.8 percent in 1960). New York City's expenditures and revenues are so large that they tend to dominate the average in any grouping in which they are included.

Historical Background

The property tax began as a land tax in the colonial period. Additions of personal property—both tangible and intangible—to be taxed at the full rate resulted in the establishment of a general property tax by the time of the Civil War. Though constantly under attack because of inequities in administration, the general property tax remained the major tax source of revenue for both the State and local governments until the 1920's. By the end of that decade the general property tax had relinquished its dominant role in State finance to motor fuel and vehicle taxes as a result of the tremendous expansion in automobile production and ownership during the period.

The decade of the thirties brought the general sales tax and the income tax to such a significant number of States that the property tax was reduced in comparative yield to only a minor fraction of total revenue for State use. By 1942, the general property tax amounted to only 3.8 percent of all State revenues, as contrasted with 25.6 percent in 1922 and 42.7 percent in 1902.

This diminution in comparative yield resulted not only from the rapid growth of sales and income taxes, but also from a de-emphasis or abandonment of the property tax as a general revenue producer by State governments. This was a conscious effort on

¹ For a full statement of Bureau of the Census criteria, see U.S. Bureau of the Census, *U.S. Census of Governments: 1957*, Vol. I, No. 3, *Local Government Structure*, p. 1-5. The full citation for this and all footnoted bibliographic references which follow will be found in the bibliography appended to this study.

the part of most States to relieve the total property tax burden. The result was a shifting of the use of the property tax almost entirely to the local level of government, including schools.

Instead of using 11.6 percent of all property taxes collected as was done in 1902, States on the average today use only 3.6 percent. There are wide ranges in this use between States ranging from 0 percent to 21.7 percent, but the trend has been steadily downward. Except for the depression years of the 1930's and the year 1953, the absolute amount of the property tax collected by the States has gradually increased, largely because property values have risen faster than State property tax rates have been cut or abandoned. While not significant percentagewise, the full release of State-imposed property taxes would add over \$600 million to potential local sources, though some of the State-assessed property would pose administrative problems if local assessments were required.

Erosion of the Property Tax Base

Although the local units of government have been given a virtually clear field in the use of the property tax, the potential base of this source has been gradually reduced to a point where it is only producing a fraction of what could be obtained if its full potential were realized. In absolute terms, of course, the dollar value of the base has increased. The gradual reduction of the potential property tax base has been brought about in two ways: (1) The extension of exemptions to the tax on grounds of equity, welfare, or administrative simplicity, and (2) the deterioration of the assessable base in relation to true value either through classification or maladministration. The general property tax has evolved in the direction of a real estate tax but with serious encroachments even upon this base.

Exemptions

The general property tax has never been truly "general," meaning that it applied to all classes of property without exception and at uniform rates. Historically the property tax has moved toward and away from the ideal concept of a general property tax in different periods, but at all times the tax base has been limited by exemptions.

The two most common exemptions are those granted to: (1) government property and (2) the property of religious, educational, cultural, and charitable nonprofit institutions.

The exemption of the property of government is justified on two grounds. First, it is considered inefficient to tax property which is purchased and supported by tax money. This would be at best a pocket transfer. There has been some sentiment expressed, however, for placing government business-type enterprises on the tax rolls so that their costs and profits could be compared to private business. This could be justified on either competitive or efficiency measurement grounds depending on government's role relative to private enterprise in the same areas of endeavor. The prevailing attitude in this country that government should not be involved in business areas where private enterprise can provide adequate service removes most of the need for the competitive argument.

The second ground involves intergovernmental relations under our Federal system. The early Supreme Court decision of *McCulloch v. Maryland* stated that the power to tax was the power to destroy and that the States could not be allowed to impede the operation of the Federal Government through this device. The case hinged upon a discriminatory attempt to tax a Federal "instrumentality," the National Bank, but the prohibition was extended to nondiscriminatory as well as discriminatory taxes. The exemptions which apply to virtually all Federal holdings affect the State and local governments more than the Federal Government, even though a reciprocal arrangement with respect to Federal taxation of State instrumentalities prevails,² because the Federal Government does not use the property tax as a source of revenue.

The property of religious, educational, cultural, and charitable nonprofit institutions is exempted almost universally in the United States. There are some differences in the interpretation of what property should and does fall in these categories in different States, but all extend exemptions to some property in these areas. The justification for such exemptions has traditionally been based on one of these grounds: (1) The encouragement of activities important to society, or (2) the private fulfillment of functions which are of public benefit and would otherwise have to be provided by government at, perhaps, greater cost. In the case of religious activities, tax exemption often represents a form of subsidy which would otherwise be constitutionally prohibited but can perhaps be justified on the ground that taxation might give an opportunity for discriminatory oppression, which would be objectionable under a positive concept of freedom of religion.

² Not, however, bolstered by Court decisions but by provisions of Congress.

In addition to the more or less universal exemptions discussed above, there are a variety of other categories of exemptions used in varying degrees by different States. Real estate may be exempted in whole or in part as homesteads, veteran benefits, or as a means of encouraging industrial or business development.³ In some States these exemptions may remove sizable proportions from the real estate tax base. Homestead exemptions in Mississippi, for example, accounted for 45 percent of all locally assessed real property valuations in 1960.⁴

While there are no adequate figures to support a firm conclusion, it is sometimes estimated that between one-fourth and one-third of the real estate tax base in the United States is exempt. In many States, no figures are collected on exempt property; and where they are collected, the figures are probably undervalued. Assessing officials, who are frequently too hard pressed to do an adequate job of evaluating nonexempt property, are not likely to spend much time or effort on property which will produce no revenue. For this reason, estimates of the value of exempt property are even less accurate than those on taxed property.

The general property tax base includes all property—real estate and personalty, both tangible and intangible. This has and does involve the taxing not only of land and improvements but also household furnishings, vehicles, business equipment and inventories, jewelry and other valuables, money and bank accounts, and securities and all paper instruments of monetary value.

The intangible personal property exemption, which includes money and valuable paper instruments, is approaching universality even though these items are still taxed in a few States. Its disappearance from the tax rolls has been justified on several grounds: (1) The extreme difficulty in enforcing the tax because of the ease of concealment, making it virtually a tax on honesty, (2) double taxation on instrumentalities representing property holdings, and (3) tax rates which may become almost confiscatory relative to the income from securities.

The reasoning against the taxation of intangibles seems so strong that it is probably only the reluctance to give up any tax source without a substitute that keeps it in the few remaining States. Even where used it is a very minor part of the property tax and is usually laxly enforced.

The taxation of tangible personalty presents a different picture.

³ See, for example, Mabel Newcomer, "The Growth of Property Tax Exemptions," p. 116-128.

⁴ Arthur L. Cunkle, "The Replacement of Local Revenues Lost Through Homestead Exemption," p. 7.

Four States—Delaware, Hawaii, New York, and Pennsylvania—exempt all tangible personal property.⁵ The other forty-six States tax personal property but with varying degrees and kinds of exemptions.

Motor vehicles and household furnishings are widely exempted in whole or part, or are subject to a special property tax which may be the equivalent of a partial exemption. While there have been extensive reductions made in the tangible personal property tax base, there has been less interest in total exemption than in the case of intangible personal property. Tangible personal property still comprises a substantial portion of the total property tax base. In 1956, the Bureau of the Census reported that 17.4 percent of the locally assessed general property tax base was made up of personal property.⁶ In 1961 this figure declined to 15.9 percent.⁷ A very small portion of intangibles are included, but this is probably offset by the amount of State-assessed personal property not designated as such or included in the Census figures. Business and agriculture personalty, e.g., machinery, equipment, inventories, livestock, make up a sizable portion of the tangible base; but since this property is related to income production, many persons feel that it is as fully justified for inclusion on the tax rolls as real estate.

Inclusion of household furnishings and jewelry or other tangible valuables has been objected to, and frequently exempted, because of the difficulty in adequately administering the assessment process. Self-assessment or "courthouse" assessment, based on some percentage of real property value, has been too frequently the rule. Exemption of motor vehicles has been justified and sometimes necessitated by the other special taxes applied to them.

The variety of exemptions to both real and personal property is almost endless. One of the latest to be added in a number of States and likely to be added in others is the exemption of fallout shelters in support of civil defense. There is no end to the number of worthwhile activities, not to mention those of a questionable nature, which can be partially supported by government through tax exemptions.

The erosion of the tax base through exemption is not peculiar

⁵ Business machinery may be considered a part of real estate in some cases. Special franchises are taxable in certain New York cities, and the mixed valuation may involve aspects of tangible personal property.

⁶ U.S. Bureau of the Census, *U.S. Census of Governments, 1957*, Vol. V, *Taxable Property Values in the United States*, p. 3.

⁷ U.S. Bureau of the Census, *1962 Census of Governments, "Assessed Values for Property Taxation,"* table 1, p. 14-15.

to the property tax, but it is this base which has such significant consequences for the schools. The real question which must ultimately be faced, if the trend toward exemption increases, is whether government should support certain activities directly, protected by a periodic review brought about by the appropriation process, or whether indirect support of unknown magnitude shall continue to be given through exemption—a status rarely reviewed on merit.

Assessment Ratios

Even with the growth in exemptions, the property tax would be adequate in most cases as a source of revenue if the ratio of assessment to true or market value of property were more realistic, that is, approached 100 percent. As in the case of exemptions, the figures available to indicate the degree of underassessment of property are all subject to some criticism, but the best or most optimistic figures present a rather distressing picture. It has been the assessment practices more than any other single factor which has given the property tax such a poor reputation. These practices have been unsatisfactory for a long time and the laments of persons in the 19th century seem strangely modern when applied to property-tax assessment procedures. This is not to say that there has been no improvement, but it has only been spotty. On the basis of sample sales ratio studies made in 1956, the Bureau of the Census indicated that average real property was assessed at 30 percent of the market value.⁸ On an individual State basis the percentages ranged from 6.5 percent to 64.2 percent. Only 11 States had sales ratios of over 40 percent.⁹ The variations in the assessment of individual properties as compared to true value is extremely broad, ranging from zero or total omission to over 100 percent—sometimes several times the value of the property.¹⁰

The ratio of assessment to true value for personal property is much more difficult to determine and is based largely on estimates of total personal property wealth as compared with the assessment rolls. Since personal property transactions are not controlled and recorded like real property, there is no easy way to compare real value with assessed value for individual items.

⁸ U.S. Bureau of the Census, *U.S. Census of Governments, 1957*. Vol. V, *Taxable Property Values in the United States*, table 2, p. 81.

⁹ *Loc. cit.*

¹⁰ Some indication of the variation may be seen in the figures for the coefficients of intra-area dispersion developed by the Bureau of the Census, *ibid.*, p. 12-13 and table 22.

Administrative omission from the tax rolls is more prevalent in personal than real property; and except in the case of bank accounts and negotiable securities, the valuation of personal property is a more difficult technical task than with real property. The smaller role of the personal property segment of the general property tax achieved through legal exemption has possibly reduced interest in higher ratios. All of these things result in a much lower *average* ratio of assessment to true value for personal property. Mabel Newcomer estimated the ratio at 10.9 percent in 1948 as compared with 30.5 percent for real property. In 1902, however, when personal property played a more significant role in the general property tax base, the ratios were estimated at 31.3 percent for personal and 38.8 percent for real property.¹¹

Once again, as in real property, the variations between ratios in States and between classes of property is extreme. Business personalty, for example, which is easier to locate and evaluate, less "personal," and more significant in value, will in most cases be assessed at higher ratios than household personalty, where taxed.

The problem of assessment ratios involves both the size of the property base and equitable application of the tax. The wide variance in the ratios may be more significant from the latter point of view than the former, since adjustments in tax rate can compensate for a lower base except where tax limits apply. Varying ratios of assessment can result from incompetent assessment, lack of adequate assessment personnel to keep current the evaluations, political pressure or favoritism, arbitrary judgments or tacitly recognized attempts by the assessing official to evaluate the economic status of the taxpayer and grant relief in the form of low assessments for widows, the aged, special businesses, or others.

Classification

While none of these reasons are acceptable explanations for varying ratios from the point of view of equity, there is a body of thought which maintains that different types of property should be taxed on the basis of different values. This has led to two approaches within the States in order to give legal status to variations which have occurred in practice, though on a haphazard basis, and to avoid variations in practice. One approach has been

¹¹ Mabel Newcomer, "The Growth of Property Tax Exemptions," table 6, p. 46.

to select certain property, e.g., grain or intangibles, and apply a special tax rate to it, usually lower than the general rate. In the case of grain, the rate is based on volume rather than ad valorem. One State, West Virginia, has created four classes of property, each bearing a separate tax rate limit.

Another approach has been to classify property according to type and apply different ratios of assessment, e.g., 100 percent, 40 percent, 30 percent, 25 percent, to the different classes of property.¹² The basis of the percentage awards to each class will ordinarily defy economic description. Several States have gone from full value to a fractional assessment of all property, e.g., 25 percent or 50 percent, without classifying.

While the purpose of classification schemes is to create a more equitable property tax, there is no evidence to show that this has resulted in practice. In the case of tax limits for various classes, the net result is generally to lower the tax yield, though some feel that a low fixed rate in the States that use it brings more extensive reporting of intangibles on the tax roll, thus providing greater equity for this class of property. Where fractional assessments are used, the picture is simply further blurred and the difficulties compounded by superimposing fractional assessments on widely varied and low original valuations. To the problem of achieving greater equity in assessments, there is no substitute for sound professional assessment practices. Too few communities have been willing to adopt and support these practices.

One of the greatest effects of fractional assessments, whether legally or administratively imposed, is the destruction of any sound basis for determining equality of assessments. While in theory it should not make any difference in the question of equality whether assessments are at 40 percent, 100 percent, or 200 percent of true value, in practice the average homeowner is not going to be able to judge the accuracy of his assessment when it varies widely from market value. Fractional assessments offer a frequent advantage to the assessor in that the courts usually reduce any assessment shown to be slightly over full market value, but frequently tolerate wide ranges of estimates of fractional values—perhaps unreasonable, but an important fact of life to the assessor, who naturally is interested in avoiding complaints or the contesting of his assessments.¹³

¹² This practice is used, for example, in Minnesota and Montana.

¹³ Some judicial relief for taxpayers overassessed though within the statutory requirement of full value may be forthcoming if recent decisions in New Jersey and Illinois are expanded. See William Kingsley, "New Standard for Judicial Relief from Discriminatory Property Tax Assessments," p. 27-31.

Summary and Conclusions

The general property tax base has been eroded through exemptions and fractional assessments to a point where it represents only a small portion of its potential in terms of true value. This erosion has partially been a result of definite legislative policy but has also been accelerated by the tremendous rate of growth of property values in the post World War II period. Understaffed assessors' offices have frequently been unable to reevaluate property to keep up with this growth. The pressure to do so has been reduced by the addition to the tax rolls of new properties which are easily assessed, thus giving the appearance of substantial growth even though the new property added at reasonable valuations may gradually decline in relation to true value because of the lack of reassessment.

That the tax base has not increased in proportion to government obligations is indicated by the rise in tax rates which have with increasing frequency been reaching statutory or constitutional rate limits.¹⁴ While the limits can and have been raised, these limits make the property tax more difficult to apply.

Since the States have shifted to other sources of revenue and the Federal Government, for various reasons, has never made any continuous or recent use of this tax, it is the local units of government which are most affected by these events. Further, the schools, which dominate the local picture, are, in general, more severely affected than the other local units which receive the bulk of local nonproperty taxes.

¹⁴ While not oriented specifically toward school districts, a recent survey of the Advisory Commission on Intergovernmental Relations reports that of 26 States able to provide data from the 42 States that have property tax limitations, 10 States indicated all or most of their local jurisdictions at the legal limit; 2 States, that none of their local governments were at the legal limit; and in the remaining 14 States, the range of local units at the legal limit extended from a few to 40 or 50 percent. See *State Constitutional and Statutory Restrictions on Local Taxing Powers*, p. 69.

CHAPTER 2

Future Revenue Sources for Schools

FINANCE PATTERNS for support of the public schools in the future will have an important bearing upon the tax sources which are used for this purpose, and the necessity or lack thereof for nonproperty taxes. While the property tax will unquestionably remain an important source of school revenue in the foreseeable future, the degree of its importance and the emphasis which is placed on local nonproperty sources may be closely tied to inter-governmental aid patterns.

An increase in the percentage of State aid for local schools automatically brings into the picture additional nonproperty sources, since most State taxes are nonproperty taxes, e.g., sales or income taxes. A decrease in State aid on the other hand may mean an increased burden on local sources, primarily the property tax, and encourage a shift to local nonproperty sources. The same could be said of Federal aid programs, though the percentage of such aid is today relatively small and a discussion of future effects might fall largely in the realm of speculation. Let us examine, however, the future possibilities for the property tax, State aid, and local nonproperty taxes while bearing in mind that any future Federal aid programs might have effects similar to increased State aid programs, at least with respect to local nonproperty taxes, though drawing from a much broader base.

Property Tax

In spite of the disadvantages of the property tax which have already been discussed—inadequate administration, erosion of the base, and questionable equity—there are many who feel that it remains the most acceptable tax for local use by school districts.

One writer, in dealing with taxation for schools, devotes many pages to analyzing and defending the property tax. While calling for reforms, he maintains that the property tax should remain a basic source of revenue for the schools.¹ Other authors, con-

¹ Roger A. Freeman, *Taxes for the Schools*, *passim*.

sidered more friendly to the schools, writing in the area of school finance also support the continued use of the property tax, though preferably with reform.² One textbook indicates that:

... The property tax must be retained for local school support if the policy of providing for local participation in public school financing is continued.³

A recent study in financing public education concludes that "the property tax is a far better fiscal instrument than most of its critics have allowed."⁴ The author of the study is, consistent with his support of the property tax, unenthusiastic about local nonproperty taxes for public education.⁵

Why do so many authors in the area of school finance support the property tax and ask for reform rather than abolition? Stability of yield is one factor that is almost always emphasized, and this is generally true except during severe depressions.⁶ Studies have shown that the elasticity of the property tax is not as great as that of consumption or income taxes,⁷ but this affects decreases in yield as well as increases. In other words, low elasticity equals high stability.

The property tax is peculiarly adaptable to school districts of all sizes from the point of view of administration. This is true for at least two reasons. With real property dominating the tax base, this wealth is easily identified, relatively permanent, and does not ordinarily change rapidly in value. Secondly, the tax is normally administered by another level of government with the school district setting the rate for the property within its boundaries. That this easy administration is often poor administration is too frequently overlooked by the schools. The irregular distribution of property between school districts, though a problem, is partially overcome by State-aid programs which further ameliorate pressures to improve the base.

Though few would defend the obvious inequities in the administration of the property tax, it is pointed out that many of these inequities have already been capitalized into the property values, thus creating problems for any revolutionary change in admin-

² See Paul R. Mort, Walter C. Reusser, and John W. Polley, *Public School Finance*, p. 130-131; Arvid J. Burke, *Financing Public Schools in the United States*, p. 262-298; and W. Monfort Barr, *American Public School Finance*, p. 110-127.

³ Roe L. Johns and Edgar L. Morphet, *Financing the Public Schools*, p. 200.

⁴ Jesse Burkhead, *State and Local Taxes for Public Education*, p. 70.

⁵ *Ibid.*, p. 98-101.

⁶ For comment on this and illustrations of retained stability in a local depression, see Charles S. Benson, *The Economics of Public Education*, p. 171-173.

⁷ See Eugene P. McLoone, "Effects of Tax Elasticities on the Financial Support of Education," table 25, p. 128 and sources listed. Also Selma J. Mushkin, "Population and Public Finances," p. 83.

istration. For example, increased property taxes will tend to reduce the sale value of property and decreased taxes raise such value. Any drastic change in assessments would result in windfalls or losses to the current owner, depending on the direction of movement.

Finally, it is noted that the amount of yield of the property tax is so great that no full substitute for it could be found which would not present problems and inequities, different, but equally as severe, as the property tax.

While emphasizing the inevitability or desirability of a continued property tax role, most supporters contend that there is a need for reform and improvement. The recommendations take many forms but always emphasize an improvement in assessment practices.⁸

In addition to the obvious need for more current and accurate assessments, there are other suggestions which have been offered to improve the property tax or make it more palatable. The size of the tax bill is one important drawback to the property tax. While many persons buying homes have a "pay-as-you-go" or withholding feature by including an amount for taxes in the monthly payment to the mortgage holder who in turn takes care of the taxes when due, most homeowners are faced with a sizable bill once or twice a year. While this total bill is ordinarily small compared to income tax payments, it may be the only tax bill they see directly because of withholding features for income taxes and hidden or inclusive prices involved in sales and excise taxes. Their reaction may thus be out of proportion to the bill, but it is the only tax they can directly protest and in many cases vote against. Retired persons who pay little but property taxes and have no children in school may be even more critical in their reaction. The increasing numbers of such persons may have a future impact on school finance patterns.

Electronic processing has made possible the use of quarterly, bimonthly, or monthly bills which would reduce this impact at reasonable cost, particularly for the larger jurisdictions. Monthly or periodic prepayment plans such as the purchase of tax certificates at local banks have been introduced, but none of these plans can, of course, match the convenience of withholding under the income tax or even the sales tax payment procedure.

Improvements in property tax administration are technically feasible to the point of making this tax equitable within the pro-

⁸ See, for example, Frederick L. Bird, *The General Property Tax: Findings of the 1957 Census of Governments*, p. 77; and James A. Arnold, Jr., "Improving the Property Tax," p. 59-64.

visions of enacted laws. Legal inequities are a separate problem and questions of basic equality on economic grounds, in comparison with other taxes, can perhaps never be satisfactorily answered; but there is no question that improved administration would go far in enhancing the role of the property tax.

Increased State Aid

Whatever defense may be made of the property tax, the fact is that it has been playing a lesser role in the financing of schools. This has resulted primarily from the increase in State support for public schools during this century with additional minor help in percentage terms from the Federal Government. As the non-local portion of school revenues has increased, the reliance of the nonlocal governments on the property tax has declined so that by 1960 only slightly over 52 percent of estimated revenue for public elementary and secondary schools was derived from the property tax.⁹ The percentage for 1957-58 was slightly over 54 percent, while in 1912 over 82 percent of school revenue came from property taxes.¹⁰

The decline of property tax domination in the financing of elementary and secondary education follows the increase in State support of local schools which rose from almost 19 percent in 1902 to slightly over 36 percent of expenditures in 1957.¹¹ As indicated earlier in this chapter, the States' reliance on the property tax as a source of funds was also declining rapidly during this period.

Actually, the percentage of State support and the percentage of total public elementary and secondary support which the property tax represents have stabilized in the past decade. This has apparently occurred because the property tax base has grown relatively as fast as school expenditures and the State portion has only managed to hold its own percentagewise. Much of the earlier State aid was justified as relief for the property tax and many States have all or portions of their sales or income taxes earmarked for schools. The present 40 percent average support of the State comes almost entirely from nonproperty sources.

One of the persistent questions remaining is whether the prop-

⁹ Albert R. Munse, *Revenue Programs for the Public Schools in the United States, 1959-60*, table 3, p. 7.

¹⁰ Computed from Department of the Interior, Bureau of Education, *Statistics of State School Systems 1917-18*, table 58, p. 156-151; and U.S. Bureau of the Census, *Historical Statistics of the United States, Colonial Times to 1957*, Series H247, p. 208.

¹¹ U.S. Bureau of the Census, *U.S. Census of Governments, 1957*, Vol. IV, No. 3, *Historical Summary of Governmental Finances in the United States*, calculated from tables 4 and 5.

erty tax has been sufficiently relieved. The picture varies extensively between States, with Nebraska, Iowa, and New Hampshire deriving over 80 percent of their school revenue from the property tax and Hawaii, Delaware, and New Mexico deriving less than 13 percent. The amount of State aid in these instances is reversed with Hawaii, Delaware, and New Mexico providing over 70 percent State aid and Nebraska, Iowa, and New Hampshire providing 11 percent or less. The influence of State aid on property tax relief is readily seen from these illustrations.

Only 15 States in 1959-60 supplied half or more of the elementary and secondary revenues, and this includes one, Texas, where 5 percent of the State revenue was from the property tax. Using a range of from 45 to 55 percent State aid to indicate a practical balance between State and local support, it is discovered that only seven States fall within this range, though one misses by only 0.8 of one percent. These 7 or 8 States include only 4 that were not in the 15 above 50 percent.¹²

From these figures it can be seen that a maximum of 19 States have reached what might be considered a practical balance or above. The raising of the State share in the remaining States to the 45 percent or above level would reduce considerably the percentage reliance upon the property tax nationwide.

Expenditures for highways, welfare, and health present strong noneducational competition for State money, but even within the broad field of education there is competition. States have been more actively involved in the direct support and operation of institutions of higher learning than they have in elementary and secondary education, though not in total sums of money spent. Increasing future demands for higher education may therefore adversely affect the possibility of increased State aid for elementary and secondary education.

In addition to the competing demands for State money which may vary from State to State, there are major blocks to increased State aid to elementary and secondary education which result from: (1) a reluctance to adopt statewide nonproperty taxes or increase their rates to the point necessary to support additional programs, (2) a conflict of philosophy on the relationship of local support to local control of education, and (3) the opposition of those who oppose almost all government spending or increases. One frequently is used as an excuse for the others, but the combination of forces is apparently sufficient to hold down the level of such aid in most States.

¹² Albert R. Munroe, *Revenue Programs for the Public Schools in the United States, 1959-60*, table 8, p. 7.

If there were to be a rebirth of interest in increased State aid, there would, without question, be a decrease in interest in the possibility of using local nonproperty taxes for schools, the major concern of this paper. The statistics on State aid and the evaluations of persons close to the seats of action¹³ would seem to indicate that no such change in the direction of increased State aid is imminent, and further consideration of local options would therefore be appropriate.

Local Nonproperty Taxes

The remainder of this study will be devoted to a consideration of various alternatives in the field of local nonproperty sources and their actual and potential application to school finance. At this point, however, a discussion of possible approaches to their application is warranted so that it will not have to be introduced as a complicating factor at each point in the material developed later.

It can be said with certainty that any tax which can be applied at the local level can also be applied at the State level. This immediately presents an alternative as to whether the tax should be locally administered or State administered. For purposes of this study, the problems of local administration will be considered in each case. In some instances, however, it may be found that the local unit is not of an optimum size for the most efficient administration of certain taxes.

Shared or Supplemental Taxes

The existence of local units of less than optimum size does not mean that the tax could not be used, but simply that the application should come from a higher, more effective administrative level. Instead of local administration, a county-wide nonproperty tax distributed back to the source of collection or a statewide tax handled in the same way would be illustrations of alternatives.

As an example of a possible alternative, the Wayne County Association of School Boards, in October 1961, proposed that the State of Michigan authorize the formation by referendum of school district federations of all of the districts within a county or counties for the purpose of levying taxes and distributing the revenues from such levies to the school districts. A special dis-

¹³ Based on interviews with numerous persons in school and finance-related positions, State, local and private, in selected States in all regions of the United States.

tribution formula was proposed and authorization for some or all of eight local nonproperty taxes requested. This would, in essence, represent a metropolitan approach to school finance.¹⁴

In another approach, an optional feature can be introduced allowing a school district to participate in a countywide or statewide tax through a supplemental rate administered by the higher unit. An illustration of this procedure, though not applying currently to school districts, is the optional supplemental sales tax rate allowed for cities and counties in California, Illinois, and Utah, and cities in Mississippi and New Mexico. The supplemental taxes are collected by the State and returned to the cities or counties.

The choice of these approaches would not solve all administrative problems since, for example, it is necessary to keep records on collections in each participating unit. It should be emphasized that only taxes returned to the area of collection in proportion to collection are being considered here because if any other basis is used for distribution, the emphasis is shifted to the concept of equalization through an areawide tax. Although the latter is an acceptable and in many cases a desirable approach, it is one which involves different considerations from the selection of a tax alone.¹⁵

Statewide or countywide taxes have many advantages. They generally comprise a more effective administrative unit and allow for a greater uniformity of application. They further avoid some of the problems of evasion and, on a statewide basis at least, reduce some competitive situations. On the other hand, they apply to all areas and this may raise political opposition from districts or regions that do not desire or need such taxes.

There has apparently been little enthusiasm for State-shared taxes among school finance people or educators generally. This is understandable because shared taxes do not necessarily relate directly to educational need. Preference seems to be for State grant programs supported by statewide nonproperty taxes. The concept of equalizing educational opportunity is strong, and it is recognized that only the grant programs, whether through per pupil payments or "equalization" adjustments, can supply the

¹⁴ Wayne County Association of School Boards, *Report of the Study Committee on Future Revenue for Public School Financing*. For background and analysis of the Report see William J. Emerson and William Simmons, "The Case for a Metropolitan Area Taxing Unit," p. 73-79.

¹⁵ See James A. Maxwell, *Tax Credits and Intergovernmental Fiscal Relations*, chapters 6 and 7 for a discussion of the application and effects of various devices for extending intergovernmental aid—tax sharing, tax supplements, tax deductibility, tax credits, unconditional grants, and conditional grants. While oriented to the Federal-State situation, much of the argument could also apply to the State-local situation.

money to make up for the differentials in wealth between school districts. State-shared or county-shared taxes only provide a new basis for tapping the locally existent wealth.

A number of States use the device of shared taxes to support general local government services.¹⁶ Some of these taxes may be earmarked for schools or directly aid the schools if they operate under a dependent system that derives funds from a unit of government participating in State sharing for general purposes. They may indirectly benefit if the State sharing helps the other local governmental units to avoid or reduce their use of the property tax.

While the emphasis on State sharing seems to be declining, it is still a widely used device which may have political advantages in certain States. It may be that the only way certain local units can get authority to tax nonproperty sources would be through a statewide tax, locally shared.

Conclusions

It is not difficult to make a short range prediction relative to changes in the tax structure because the pattern of change is usually quite slow. The property tax is certain to remain the major source of local school revenue for some time to come. Since the property base in most areas does not seem to be growing as rapidly as tax needs, the increased tax levies on property will produce increased resistance and pressure to move to other sources. Whether relief of this pressure will come through increased State grants, State sharing arrangements, or additional provisions for local authority to levy nonproperty taxes will vary from State to State. National statistics would seem to show that increased State grants for schools are at best only holding their own with rising expenditures.

The Tax Foundation has noted that:

... since some of the pressures on State budgets come from State aids to local governments, the burden of local property taxes and the possibility of granting localities some authority to levy local nonproperty taxes must be reviewed in many States."

¹⁶ Precise figures on shared taxes versus grants are difficult to establish because the Bureau of the Census no longer distinguishes between them. It groups only on the basis of the purpose of the State distribution. Detailed information for each State is available in Vol. IV, No. 2 of the *U.S. Census of Governments, 1957* entitled *State Payments to Local Governments*. By shared taxes we mean taxes which are levied and collected by a higher unit of government and then returned in whole or in part to the subordinate units in direct proportion to the collection from that subordinate unit. See p. 21-22 in chapter 3 for further explanation.

¹⁷ *Tax Review*, October 1961, p. 40.

A 1961 study of the fiscal problems of the large cities in supporting education gave mild support to the role of local nonproperty taxes by stating:

In some cases much improvement in support can be accomplished by adding new avenues of direct local taxation. Local tax leeway for education is suffering from almost sole dependence on the property tax base. The provision of some access to local taxes on transactions and income bases might give a much needed boost to local initiative.²⁸

On the assumption that more interest in the possibility of local nonproperty taxation will occur in the future, this study examines current practices and possible adaptations of these taxes in the pages that follow.

²⁸ William P. McLure, coordinator, *Fiscal Policies of the Great Cities in the United States*, p. 68.

CHAPTER 3

Present Status of Nonproperty Tax Use by School Districts

WHILE LOCAL nonproperty taxes make up only a small portion of total revenue for the schools, an examination of the present use in some detail along with the other sources of revenue should prove useful and is, indeed, necessary before an effective evaluation of the potential can be made. Exact information on the extent and amount of such taxes for school use is not available for two reasons: (1) The small sums of money involved do not warrant a special national survey, and (2) the amounts involved in fiscally dependent school systems would have to be imputed under any circumstance. Use will be made of available Bureau of the Census and Office of Education figures as well as State reports in those States where such use is significant.

Local Nonproperty Taxes

According to the *1957 Census of Governments*, nonproperty taxes used by local governments for all purposes, including schools, amounted to only \$1.9 billion out of a total of \$14.3 billion for all local taxes. That the use of such taxes is somewhat disproportionately spread is illustrated by the fact that four States and the District of Columbia account for 61.3 percent of all local *nonproperty* taxes while accounting for only 37.1 percent of all local taxes.¹ The disproportionate distribution for fiscally independent school districts is even greater with one State, Pennsylvania, accounting for \$58.7 million out of a total of only \$63.1 million of nonproperty taxes used by these school districts.²

¹ U.S. Bureau of the Census, *U.S. Census of Governments, 1957*, Vol. III, No. 5, *Compendium of Government Finances*, table 23.

² U.S. Bureau of the Census, *U.S. Census of Governments, 1957*, Vol. III, No. 1, *Finances of School Districts*, table 2.

Shared Taxes

The Bureau of the Census does not include shared taxes in its estimates of local nonproperty taxes except where the rate is specifically set by the local unit. Shares of State taxes paid back to the local unit even on the basis of the collection are considered as intergovernmental revenue. While it is admittedly difficult in some cases to distinguish between a shared tax and a grant,³ the distinction does become important when local sources of revenue are being examined from the local viewpoint. A State tax imposed on the local unit and returned on a pro rata basis becomes the equivalent of a local tax which would produce the pro rata share. In both instances the impact of the tax is the same—the taxpayer of the local unit—and no equalization or redistribution is involved. The only differences are in the lack of local option and possibly in the cost of collecting the tax. To illustrate this situation, in Maryland the proceeds of a rate equal to 0.68 percent of taxable income out of the total State tax of 3 percent⁴ is distributed back to the cities and counties of origin. This is exactly the same as a local tax of 0.68 percent using the same inclusions and exclusions of income as the State, yet the former would not be counted as local revenue, while the latter would.

Fiscally Independent School Districts

In the case of the independent school districts, this procedure is of little consequence because the amount of "shared" taxes is small. There is some indirect sharing through counties as in Oklahoma where motor vehicle licenses and severance taxes shared with the counties provided \$23,481,000 or \$47.92 per enrolled child in 1957. This money is shared with the counties, which are, in turn, required to distribute the funds on an average daily attendance basis to the school districts. The money is shared to the county of origin but issued on a flat grant basis to the school districts. While this is a true sharing program under our definition with respect to the counties, the individual school district may get a larger or smaller share than it would if the money were paid directly to the school district of origin. The only substantial share to an independent school district directly was the

³ For example, Wisconsin distributes a portion of its individual and corporate income tax to cities and counties of origin but only to a maximum amount receivable by any one city or county. For those cities or counties under the maximum, it is a true sharing arrangement, but the ceiling has the effect of changing the sharing rate for the larger or wealthier jurisdictions.

⁴ Investment income involves a distribution of 1.70 percent out of a 5-percent State tax.

payment of a portion of the State individual and corporation income taxes collected in Milwaukee, \$2,076,000 in 1957, for the Milwaukee teachers' pension fund. All other shared taxes with independent school districts amounted to only \$779,000.⁵

Fiscally Dependent School Districts

When the use of nonproperty taxes by dependent school systems is examined, the sharing arrangement becomes more significant. Analyzing the Bureau of the Census' detailed presentation of *State Payments to Local Governments*⁶ on the basis of a different set of standards for defining shared taxes,⁷ one finds that approximately \$319 million in 1957 could be attributed to local sources of nonproperty revenue. This would increase our original estimate for all local government nonproperty taxes to \$2.22 billion out of a total of \$14.62 billion. Of this additional \$319 million, approximately \$143 million is distributed to governmental units which have dependent school systems.

Since approximately 20 percent of the expenditures for local schools in 1957 was attributed to other than independent school districts, the role of the dependent school district cannot be ignored. We are concerned with the potentialities of the nonproperty tax for all types of school districts, large and small, urban and rural, dependent and independent. Since revenue figures for school systems in dependent situations are not computed and collected separately from the other local unit involved, it is necessary to estimate and impute figures from available data to derive some picture of the nonproperty tax role.

On the assumption that in a truly dependent situation the tax sources would be mingled, calculations were made for each of the 20 States and the District of Columbia which the Bureau of the Census has indicated have a partial or fully dependent relationship for school systems. Since the ratio of expenditures for local schools to total direct general expenditure should represent an approximate share of the general treasury and revenue which schools could expect, such ratios were applied to the local nonproperty taxes of each type of local government involved with

⁵ On the basis of analysis as explained below.

⁶ U.S. Bureau of the Census, *U.S. Census of Governments, 1957*, Vol. IV, No. 2, *State Payments to Local Governments*.

⁷ If the proceeds of a tax are returned to the local government in proportion to the collections of the tax in the local unit or on a basis which could be used for collecting it, the tax will be defined as shared. This is broader than the Bureau of the Census definition which requires the local unit to actually set the rate of the tax being collected by the State or higher unit.

school systems in each State and the District of Columbia. Shared taxes were added to the above local nonproperty taxes and a figure of approximately \$246 million was obtained which represents the *theoretical* value of nonproperty taxes to dependent local school systems. This is over four times the amount of nonproperty taxes locally raised by the independent school districts, which account for 80 percent of the expenditures for public elementary and secondary education in the United States. What we see here is an obverse ratio, not unexpected, which further illustrates the role of the property tax in education. It is the noneducational functions which have drawn the nonproperty authority and sources to the local units of government, excluding school districts; and it is only theoretical calculations such as these which can add any substantial local nonproperty taxes for schools.

Emphasis must be made that these are *theoretical* values for the dependent school systems. Actually many "dependent" school systems are not dependent except legally and the legal provisions are frequently limited, or not used by the controlling level of government. The City Council of St. Paul, Minnesota, for example, may legally raise or lower school budgets but has never exercised this authority. Further, there is no intermingling of school funds with the other local funds, and local revenue for the schools is provided by special property tax millage authorizations included in the city charter.

The separation of funds is common even in those dependent situations where the local government above the school board does exercise some budgetary control in practice. Local school funds may be derived from special millage levies rather than appropriations from the general treasury, or the property tax bill may indicate a specific portion of the rate, normally the largest, as going to schools even if they operate on an appropriation. It would be an exceptional situation to find a school system which is treated on the same basis as the other departments of local government. This arrangement has both its advantages and disadvantages. The effect on the subject matter of this study is that for all intents and purposes the rather sizable proportions of nonproperty taxes collected at the local level in many dependent situations do *not* accrue to the benefit of the schools psychologically. There may, of course, be some indirect benefit through relief from the additional property tax levies which would occur without the local nonproperty taxes.

In summary, we can see that, while the dependent school system may in theory draw greater support from local nonproperty

taxes than independent school systems, in practice and psychologically, both types of systems are stereotyped as deriving almost total local support from property taxes. Where the local nonproperty sources are clearly marked as going to schools, the sums of money involved are generally small. The State of Pennsylvania becomes the exception to this rule and the districts in this case are independent.

Effect of District Size

In order to determine whether there is any tendency for States within a particular category of school district structure to utilize local nonproperty taxes more than others, a comparison was made between average enrollment and average local nonproperty tax per pupil.

Independent Districts

According to Bureau of the Census figures for 1957 (as of October 1956), the average enrollment for independent school districts among the States ranged from 43 to 10,851. The national average was 485.

By examining table 1 one can note that of the 18 States listed as receiving local nonproperty taxes, levied or shared, only 5 fall below the national average of school district size. The total amount for Wisconsin, it should be noted, goes to the Milwaukee school district, which is well above the national average in size even though the average size of the school districts in that State is below that of the rest of the Nation.

While it may appear that States with large school districts are more inclined to utilize local nonproperty taxes for schools, there are sufficient States with below or average size school districts to moderate any very strong conclusion. Pennsylvania, the State making greatest use of these taxes, would not be classified as a large district State in organization terms. Sixty percent of the school districts in Pennsylvania had enrollments of under 150 in 1956. As a matter of fact, in 7 of the 18 States involved, over 50 percent of the school districts had enrollments of less than 150. The national average is sharply affected by the large number of very small school districts in the United States; the average is therefore not in any sense considered an optimum size. We cannot conclude that those States which have reorganized into more effec-

Table 1.—States in which independent school districts receive local nonproperty taxes: 1957

State	Number of districts	Average enrollment	Average local non-property taxes per pupil ¹
Total ²	50,895	485
Alabama ³	112	6,366	\$.39
Alaska ⁴	8	2,250	7.44
Arkansas ⁵	423	917	1.29
Delaware.....	15	1,867	5.75
Indiana.....	1,030	826	.43
Kansas.....	3,140	130	.76
Kentucky.....	221	2,670	.73
Minnesota.....	3,464	162	.95
Mississippi.....	79	2,152	1.46
Nebraska.....	4,942	54	1.63
Nevada.....	17	2,941	.50
New Mexico.....	95	1,884	.15
New York.....	1,664	793	1.05
Pennsylvania.....	2,858	639	32.17
South Carolina.....	107	5,112	.38
Vermont.....	16	563	2.78
Wisconsin ⁶	3,758	109	5.05
Wyoming.....	246	280	2.67

¹ This is an average derived by dividing total enrollment into local nonproperty tax receipts and should not be construed to mean that all districts are actually using such taxes.

² A total of 44 States had independent school districts in 1957.

³ Shared taxes. In Wisconsin only Milwaukee shares.

⁴ Not included in 44-State average since it was not a State in 1957.

SOURCE: U.S. Bureau of the Census, U.S. Census of Governments, 1957, Vol. III, No. 1, Finances of School Districts, tables 2, 6; and calculations on shared taxes as indicated in chapter 3 of this study.

tive and efficient districts have moved in the direction of local nonproperty taxation.

Dependent Districts

The picture is even more variable with respect to the dependent school districts if the theoretical values developed earlier are used. This situation illustrates more than anything else the wide variety of practices between States in granting local nonproperty taxing powers to units other than school districts. Table 2 lists the States with dependent school systems in order of average size of systems accompanied by the average local nonproperty taxes per pupil. The fact that there is little direct relationship between the aver-

Table 2.—Comparison of 20 States with dependent school systems by average enrollment size of districts and average local nonproperty taxes per pupil: 1957

State	Average enrollment per district	Average local non-property taxes per pupil
New York.....	182,900	\$109.40
Hawaii.....	123,100	16.15
Maryland.....	21,112	44.53
Delaware.....	19,300	8.32
Texas ¹	9,643	15.33
North Carolina.....	5,876	2.31
Virginia.....	5,773	20.87
Tennessee.....	5,305	11.67
New Jersey ¹	4,926	57.94
Mississippi.....	4,057	12.43
New Hampshire.....	3,122	16.65
Minnesota.....	3,120	21.65
Rhode Island.....	3,021	7.68
Connecticut.....	2,300	8.42
Wisconsin ¹	2,257	85.18
Massachusetts.....	2,212	6.14
Alaska ¹	729	30.20
Maine.....	390	4.21
Arizona ¹	267	396.25
Vermont.....	262	8.12

¹ Less than 50 percent of the pupils enrolled in dependent systems.

SOURCES: U.S. Bureau of the Census, U.S. Census of Governments, 1957, Vol. III, No. 1, *Finances of School Districts*, p. 8; Vol. III, No. 5, *Compendium of Government Finances*, table 46; and calculations made by author.

age size of district and the amount of nonproperty taxes per pupil is readily seen. In dependent school districts, however, no relationship would be expected, since the nonproperty taxes involved are related generally to functions other than education, and any direct relationship would be accidental.

State Aid and Local Nonproperty Taxes

Since State aid is sometimes justified as a means of broadening and diversifying the tax base, an examination of the relationship of State aid to the use of local nonproperty taxes was made to see if there was any indication that States were using local nonproperty taxes in lieu of State aid. Such does not appear to be the case and, as a matter of fact, the reverse appears to be true. In table 3 one can note that, of 18 States with independent school

Table 3.—Ranking of 18 States with independent districts by average percent of State aid and average local nonproperty taxes per pupil enrolled: 1957

State	Average State aid (percent)	Average local nonproperty taxes per pupil
Delaware.....	93.5	\$5.75
New Mexico.....	73.8	.15
Alabama ¹	70.5	.39
South Carolina.....	66.5	.38
Alaska.....	64.9	7.44
Mississippi.....	54.4	1.46
Arkansas ¹	50.8	1.29
Pennsylvania.....	48.4	32.17
Kentucky.....	47.9	.73
Nevada.....	46.2	.50
Wyoming.....	44.7	2.67
Minnesota.....	42.8	.95
New York.....	39.5	1.05
Vermont.....	33.0	2.78
Indiana.....	31.3	.43
Wisconsin ¹	21.2	5.05
Kansas.....	20.1	.76
Nebraska.....	6.8	1.63
18-State median.....	47.0	1.17
48-State mean.....	41.1	^a In
48-State median.....	37.6	^a In

¹ Shared taxes.

^a Inapplicable.

SOURCES: U.S. Bureau of the Census, U.S. Census of Governments, 1957, Vol. III, No. 1, Finances of School Districts, tables 2 and 6; Albert R. Munoz and Eugene P. McLoone, Public School Finance Programs of the United States, 1957-58, table 2; and calculations on shared taxes as indicated in chapter 3 of this study.

districts using local nonproperty taxes in 1957, 12 States provided aid above the national mean for that year. Included in this group was Pennsylvania, the only substantial user. New York was not included but fell close to the mean at 39.5 percent. Only five States using local nonproperty sources for schools fell substantially below the national mean. The positive relationship between high State aid and use of local nonproperty taxes in independent school districts is further enhanced by the fact that the median as opposed to mean average State aid is approximately 37.6 percent, a lower figure.

The case for school systems under dependent fiscal arrangements is not as clear cut. From table 4 one can see that 12 out of

Table 4.—Comparison of 20 States with dependent school systems by average percent of State aid and theoretical average local nonproperty taxes per pupil: 1957

State	Average State aid (percent)	Average local non-property taxes per pupil
Delaware.....	93.5	\$8.32
Hawaii.....	71.1	16.15
North Carolina.....	68.9	2.31
Alaska ¹	64.9	30.20
Tennessee.....	62.0	11.67
Mississippi.....	54.4	12.43
Texas ¹	53.0	15.33
Minnesota ¹	42.8	21.65
New York ¹	39.5	109.40
Virginia.....	36.1	20.87
Maryland.....	33.7	44.53
Vermont.....	33.0	8.12
Arizona ¹	31.8	396.25
Maine.....	30.3	4.21
Connecticut.....	27.2	8.32
Massachusetts.....	26.5	6.14
New Jersey ¹	26.1	57.94
Rhode Island.....	24.9	7.68
Wisconsin ¹	21.2	85.18
New Hampshire ¹	9.4	16.65
20-State median.....	33.4	15.74
48-State mean.....	41.1	^a In
48-State median.....	37.6	^a In

¹ Less than 50 percent of the pupils enrolled in dependent systems.

^a Inapplicable.

SOURCES: U.S. Bureau of the Census, U.S. Census of Governments, 1957, Vol. III, No. 1, Finances of School Districts, p. 8; Vol. III, No. 5, Compendium of Government Finances, table 46; Albert R. Munse, and Eugene P. McLoone, Public School Finance Programs of the United States, 1957-58, table 2; and calculations made by author.

20 States receiving theoretical local nonproperty tax support under dependent situations fall below the national mean average of State aid for education. These include New York, which is close to the average. If the median State aid is used, only 11 States fall below average. If the States with less than 50 percent dependent school systems are dropped, the picture is changed considerably with 7 out of 12 States falling below the national average.

In the case of the dependent school systems, the seemingly negative relationship, low State aid producing local nonproperty tax use, may be less significant to schools when it is remembered

that few of these local nonproperty taxes are credited to schools, except in theory. They are credited in practice to general local government.

While the above figures may not prove that high State aid is conducive to the use of local nonproperty taxes, it would certainly indicate that neither tends to limit nor preclude the other. It may well be that States which are concerned about providing additional services but avoiding an excessive burdening of the property tax are more willing to use both increased State aid and local nonproperty taxes. In the case of Pennsylvania, at least, State aid has increased at the same time that local nonproperty taxes have been expanding.

Constitutional and Legal Limitations

The use of local nonproperty taxes is related at least in a negative way to legal and constitutional provisions in the various States, since they are of course not used where there are constitutional and legal provisions against them. The absence of such legal provisions, however, does not mean that such taxes are being used.

No comprehensive survey has been made as to the actual taxing power of each State. Such a survey could only produce tentative information at best because of the judicial interpretation of such powers in the States. In general terms courts have been quite liberal in their interpretation of the powers of State legislatures in the field of taxation. Unless a tax is specifically prohibited by the constitution of the State, the legislature will be presumed to have the authority to levy such taxes as it chooses.

In the case of authorizing taxing power for local units of government, the opposite rule generally prevails. Unless there is specific authorization for the use of such a tax by constitution or law, the local unit will be presumed not to have such authority. In the case of broad grants of taxing authority by the legislature or the constitution, as in Pennsylvania's Act 481 or home rule provisions, court interpretations may still play an important role in determining just what specific taxes may be used.^a

The most comprehensive and recent survey of the restrictions on local nonproperty taxing powers was made by the Advisory Commission on Intergovernmental Relations.^b This compilation includes not only commentary on prohibitions and restrictions

^a See 84 C.J.S. Taxation §§ 4-9 for discussion and specific illustrations of State cases.

^b State Constitutional and Statutory Restrictions on Local Taxing Powers, chapter 5.

but also on authorizations for each of the major nonproperty tax categories.

Any local group considering a nonproperty tax has available through the compilation a general indication of the constitutional and legal provisions affecting adoption in a particular State. Since such compilations involve interpretations of constitutions and statutes which in many cases have not been judicially tested, no case having risen, and since statutes and constitutions are changed, more intensive analysis should be applied in each individual proposal of adoption of a local nonproperty source.

Sometimes prohibitions or limitations may be indicated in general surveys which do not exist or which may be overcome in practice. A 1955 survey of authority for a local income tax, for example, indicated that five States had constitutional prohibitions against such taxation.¹⁰ In one of the States, Maryland, two commissions in recent years have considered the possibility of adoptions at the local level and have found no such constitutional prohibitions.¹¹ The Advisory Commission study lists only two States, Florida and Tennessee, as having such specific constitutional prohibitions.

In other cases there may be statutes or constitutional provisions which indirectly affect the possibility of local nonproperty tax adoption. Prior to the 16th amendment, the Federal income tax was impractical because it was interpreted, at least partially, as a "direct" tax and, as such, had to be administered in proportion to the population of each State, thus nullifying a true income application.

Only an intensive analysis of the taxing powers granted the local unit and the possible prohibitions and limitations, direct and indirect, by statute or constitutional provision in each individual case can provide a really satisfactory conclusion for a local study group. If the proposed tax adoption represents a first effort in the State concerned, the final decision as to applicability may have to await court action.

With the above reservations emphasized, table 5 gives, by State, a summary of the constitutional and statutory limitations and prohibitions, as well as known authorizations for each of the major nonproperty sources. It will be noted that the authorizations for school district use of nonproperty taxes is extremely limited. There is more leeway for nonproperty tax use in dependent systems than in independent systems through the broader

¹⁰ Robert A. Sigafos, *The Municipal Income Tax: Its History and Problems*, p. 7-11.

¹¹ See Special Tax Study Commission, City of Baltimore, *First Interim Report*, January 15, 1957, p. 7-10; and Commission for New Revenue of Baltimore City, *Report*, 1955.

grants of nonproperty taxing power to municipalities, but, as indicated before, this is largely theoretical rather than practical. For independent school districts, it is relatively safe to conclude that legislative authorization is needed in most cases before local nonproperty taxes can be adopted. Such authorization is legally possible in most States.

Nonproperty Tax Use by Independent as Opposed to Dependent School Districts

Up to this point the consideration of nonproperty taxes has dealt with their role in both dependent and independent situations. Hereafter, the study will be concerned primarily with the role of the independent school district. This is not because the dependent school districts are unimportant but because the financing of schools under dependent situations becomes confused with the financing of other local activities even though, in practice, they are treated much more separately than the term "dependent" would imply. The problem of the dependent school system becomes one of achieving a greater acknowledgment of the role of nonproperty taxes or obtaining increased authority for the taxing unit.

Dependent school districts, if the term dependency has any meaning, must consider their role as a part of the over-all governing unit of which they are a part. The use of a particular tax will, therefore, be related not only to school but also to nonschool functions. While the economics of the situation should not vary between dependent and independent school systems, assuming the same geographic area is covered, the political factors may vary considerably. The economic factors of the independent system may frequently, however, be more complicated because the school districts do not necessarily coincide with other governmental units. Intergovernmental problems are, therefore, more evident in the independent than dependent situation.

Although dependent school districts that want to extend their use of nonproperty taxes will find much of the following material of interest, it will be more useful to the independent school districts, which wield the taxing authority.

The subject of this study is nonproperty taxation for schools and not nonproperty taxation in general. As we have seen from the analysis in foregoing sections, it becomes extremely difficult and frequently questionable to interpret the impact of particular taxes on dependent school systems. Any further references to

NONPROPERTY TAXATION FOR SCHOOLS

Table 5.—Legal basis for authorization or prohibition of major local nonproperty taxes, by State: 1962

State	Income		General sales		Busi- ness gross receipts ¹	Admi- sions	Alcoholic beverages		Cigarettes		Gasoline		Motor vehicle	Poll	Public ² utility	Real estate transfer
	A.	P.	A.	P.			A.	P.	A.	P.	A.	P.				
1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17
Alabama	S		SL		U	U	SL		SL		SL					
Alaska			SL		U	U										
Arizona	H		SL		U	U										
Arkansas	H		SL		U	U										
California			SL		U	U										
Colorado					U	U										
Connecticut			H		U	U										
Delaware					U	U										
Florida					U	U										
Georgia					U	U										
Hawaii																
Idaho																
Illinois			SL		U	U										
Indiana					U	U										
Iowa					U	U										
Kansas																
Kentucky	SL				U	U										
Louisiana			SL		U	U										
Maine					U	U										
Maryland					U	U										
Massachusetts																
Michigan	H															
Minnesota	H															
Mississippi			SL		U	U										
Missouri	SL				U	U										
Montana																
Nebraska																
Nevada																
New Hampshire																
New Jersey																

2 Key

A—Authorized
C—By constitution
H—Through home-rule powers
L—Limitations as to rate or use
P—Prohibited
S—By statute
U—Reported as used in State in 1956 but type of authority not given
•—Used by school districts
—Not known to be authorized or prohibited

NOTE: Where no State had a legal basis for prohibiting a major local nonproperty tax, the column indicating prohibitions has been omitted.

school districts or school systems, therefore, unless specifically identified as dependent, will be assumed to be independent.

Variety of Taxes

The Bureau of the Census listed a variety of nonproperty taxes in use by local school districts in its *1957 Census of Governments*.¹³ These taxes and the States where used were as follows:

Per capita or poll taxes—Delaware, Indiana, Kentucky, Mississippi, South Carolina, Vermont, and Wyoming

Dog licenses—Kansas

Business license taxes—Nebraska and New Mexico

Selective sales taxes—Nevada and New York

General sales taxes—New York

Grain handling tax—Minnesota

Mortgage registry tax—Minnesota

Pennsylvania, which accounted for \$58.7 million out of a total of \$63.1 million in nonproperty taxes collected in 1957, is not included in the above list. School districts in that State collected taxes from a wide variety of sources in 1957. These are only partially listed in the Bureau of the Census report. The nonproperty taxes most commonly used by Pennsylvania school districts are: per capita, wage and income, occupations, real estate transfer, mercantile (gross receipts), amusements, trailer, and mechanical devices.¹⁴

In addition to these there have been taxes on signs and billboards, garbage and refuse dumping, and severance.¹⁵ Taxes in the above general categories have also taken a wide variety of forms and used various rates within the limits prescribed by the legislature.

Without question, Pennsylvania provides the greatest variety and volume of nonproperty taxes used by school districts. While there have been problems in connection with such a varied approach to financing education, Pennsylvania's experience would indicate that almost any tax is applicable to some district somewhere or, in reverse logic, that some nonproperty tax is applicable in every school district in this country. One of the purposes of this study is to present information which can be used to determine what taxes can be applied to particular districts.

¹³ U.S. Bureau of the Census, *U.S. Census of Governments: 1957*, Vol. III, No. 1, *Finances of School Districts*, table 2.

¹⁴ Governor's Committee on Education, *Facts and Figures on Education in Pennsylvania, 1958-59*, p. 100-105.

¹⁵ David F. Stafford, *Financing Public Education in Pennsylvania*, p. 3; and Richard F. Schler, *The Legislative and Judicial Development of Act 481: 1947-1959*, p. 49. Severance taxes were eliminated by a legislative amendment to Act 481 in 1949.

CHAPTER 4

Analysis of Nonproperty Taxes

IN RELATING nonproperty taxes to school districts, it is important that the major features and advantages and disadvantages of the more important nonproperty tax types be understood. To do this it is necessary to establish some arbitrary groupings of taxes. It is theoretically possible to reduce all taxes to a few broad categories, for example, property, per capita, income, and sales. Going even further, it might be noted that there are only three bases for taxation—per capita, property or wealth, and monetary transactions. Since a person without property or income cannot pay any tax in money, and since one thinks of taxes in monetary terms, the true base can be simplified further. Finally, since property can only produce money through earnings or sale, the base is refined to a unitary concept of income.

Unfortunately the field of taxation is not quite so simple, and the broad base of national income is tapped through an extraordinary variety of devices and forms. This study does not propose to reform the present system of taxation, but merely to suggest how it can be adapted to meet the needs of the public schools. As a consequence, groupings are used which are rather plainly understood and differentiated in practice even though their differences in theory are not sharply definable.

Groupings of Taxes

Four broad nonproperty groupings—per capita, income, general sales, and selective sales—are used, plus a fifth miscellaneous category to take care of the few taxes which do not fit into the above nonproperty categories. The income and selective sales tax groupings are further divided into major subcategories including net income and wage or gross income in the former category, and motor vehicle, tobacco, alcoholic beverages, public utility, admissions, and miscellaneous in the latter.

"Death" taxes which include estate, inheritance, and gift taxes, are not considered in this study, primarily because they are

nowhere used in this country as a local source of revenue, except through sharing. In addition to being fairly complex to administer, as sources of local revenue they are in most cases very unstable. They do not attain much real stability until they are applied at the national level, though the wealthier States may draw a fairly regular stream of income from them. Table 6 shows the variations in yield in this category for selected States, all States, and the Federal Government in recent years.

There are some taxes which may not fit into any of these categories, but they are not taxes which we intend to analyze even though they have been used by some school districts or other local units. Illustrations of these taxes are the Pennsylvania-type occupation tax and the trailer tax. The former tax is a millage levy placed upon an individual's occupation, assessed and valued according to some established listing, ordinarily quite arbitrary; the latter is a flat monthly fee on house trailers if they parked for longer than a prescribed minimum period, in order to exclude transients from the tax. These taxes may have attributes of several of the above categories but fit into none completely. It is relatively easy to reject both of these taxes from consideration, however, because they are either closely related to the property tax, or are not widely used, or both.

It is not possible to cover all subvarieties of nonproperty taxes. Pennsylvania's school districts have tried several taxes under their "tax anything" law which have not caught on to the point of being widely acceptable even in their own State. In addition, there are a multitude of selective sales taxes which have been or could be used by local governments with proper authority. Every attempt has been made to include those taxes which have shown some significant possibilities or which have had wide local use by school districts or other local units.

Criteria for Analysis

Each tax grouping or subgrouping is examined according to four criteria: (1) Potential yield, (2) administrative feasibility, (3) equity and incidence, and (4) economic impact. In addition, some indication of the extent of use of these taxes is given at the various levels of government, since the pyramiding of taxes has become a more significant factor as the State, Federal, and local governments move into the same taxing areas.¹

¹ For a comprehensive presentation of the degree of tax overlapping, see the Advisory Commission on Intergovernmental Relations, *Tax Overlapping in the United States*.

Table 6.—Revenue from inheritance and estate taxes for selected States, all States, and the Federal Government: Selected fiscal years, 1950 to 1960
(In thousands of dollars)

State	1950	1952	1954	1955	1956	1957	1958	1959	1960
Alabama.....	\$914	\$315	\$748	\$285	\$547	\$501	\$384	\$652	\$705
California.....	18,652	27,115	23,850	28,472	34,289	35,796	42,697	42,009	43,727
Delaware.....	2,879	1,098	7,265	1,915	5,974	1,591	1,019	751	1,088
Iowa.....	3,408	3,939	5,157	4,701	4,759	5,492	7,428	6,534	7,294
New York.....	22,375	27,893	29,250	27,996	53,694	51,942	47,120	49,630	71,611
South Carolina.....	397	640	738	731	2,483	1,257	1,204	1,143	1,596
Virginia.....	1,924	2,033	1,877	3,620	2,381	3,804	3,173	3,413	4,874
All States total.....	165,631	207,158	242,650	243,704	304,571	330,245	344,446	340,928	411,151
Federal total.....	649,600	735,900	863,100	837,000	1,044,500	1,240,800	1,260,100	1,216,500	1,420,500

SOURCE: Advisory Commission on Intergovernmental Relations, Coordination of State and Federal Inheritance, Estate, and Gift Taxes, January 1961, tables A and L.

Potential Yield

The yield of a tax is a combination of rate and base less the costs of administration. The rate itself normally operates within certain limits, either legal or practical. Tax rates, whether on psychological or economic grounds, can reach a point of diminishing return. The tax would be considered excessive at the point where evasion is widely evident. While there are few, if any, absolute rules on what the rate for a particular tax should be, it is generally true that the rates of newly adopted taxes fall close to the range of rates already in use. Community pressure ordinarily requires this.

The importance of the tax base is equally apparent. Widespread exemptions not only affect the yield of a tax but may also change its incidence and economic impact. This study is concerned with the normal base for particular taxes and the modifications developed.

Administrative costs become a significant factor in yield because of the variation among the different types of taxes. For any particular tax the administrative costs are likely to vary according to such factors as the number of taxpayers, location of taxing unit, and quality of administrative personnel.

In contrast to the property tax, whose administrative costs are normally borne by the general government property tax collection system, school districts should expect administrative costs to be deducted from the yield of nonproperty taxes for their use.

Administrative Feasibility

Administrative costs are closely related to administrative feasibility, a boundary line beyond which a tax is accepted or rejected. Administrative costs represent a continuous spectrum ranging from low to high but all within the area of administrative feasibility. Excessive administrative costs, if not based simply on poor management, make a tax infeasible.

Difficulties in enforcement are also a part of administrative feasibility. Excessive evasion of a tax (and there will always be some evasion) affects not only the yield but also the equity of the tax. If administrative techniques are not available to ensure high compliance, then the tax is not feasible.

It may be possible to shift the administrative costs as measured by the expenditures of the public agency enforcing the tax to the taxpayer in certain cases, but there are limits here which, when exceeded, would make a particular tax undesirable.

Equity and Incidence

Equity can be equated with justice or the fairness of a particular tax. Attitudes about equity will be affected by "what" is taxed, "who" is taxed, and the "how" of taxation.

Incidence refers to the ultimate burden of the tax, in other words, "who" is *really* taxed. This is not always easy to determine. Only a few taxes can be said to be borne by the persons of initial impact. The degree of shifting varies, but it is important from the point of view of equity to have at least some general idea of who ultimately pays the tax.

While taxes are not paid by inanimate objects, the item taxed can have some significance from a point of view of equity. It is frequently much easier to tax items which are widely considered "less than good," e.g., alcoholic beverages, tobacco and gambling, or items that are considered luxuries. What is good or what is a luxury is, however, subject to considerable debate, particularly as the standard of living rises to the point that the luxuries of yesterday become the necessities of tomorrow.

Certain basic theories have been developed in the field of taxation to justify the imposition of certain taxes and the way they are applied. The two most prominent are the benefit theory and the ability to pay doctrine. Neither theory is clear-cut, however, and both are used very loosely to justify all types of tax programs.

Most commonly, however, the benefit theory assumes that there should be a relationship between the taxes paid by the taxpaying unit and the cost or value of the service which government supplies the taxpaying unit. The principle is easier to state than it is to apply and finds its easiest application in government enterprise type services, e.g., water, utility, transportation and postal services, where service charges rather than taxes are utilized. It has been used, however, to justify the imposition and earmarking of motor vehicle and fuel taxes to provide highways and services of major benefit to the operators of vehicles. The taxes imposed under this theory are normally proportional, but regressive taxes could be justified if the welfare functions of government were emphasized. On the other hand, progressive taxes might be justified for protection of property, assuming the wealthy have a higher than proportional stake in this area than the poor taxpayers.²

The ability-to-pay doctrine is one which is widely quoted in

² John Stuart Mill rejected the benefit view because he felt that the poor needed more protection than the wealthy and that this would require regressive taxation. Richard A. Musgrave, *The Theory of Public Finance*, p. 61.

tax literature and used primarily to support the concept of progressive taxation as applied to the Federal and most State income tax programs. Ability to pay is frequently combined in this sense with an equality of sacrifice doctrine. The assumption made is that the dollars of income are easier earned, the higher the income. For example, it is generally assumed that it is easier for a person earning \$50,000 annually to pay \$20,000, or a 40-percent tax, than for a person earning \$5,000 per year to pay \$500, or a 10-percent tax. In theoretical extremes, progressive systems may be extended to the confiscation of all income above a certain amount.

Although there are few, if any, objective measurements of the validity of such assumptions, these assumptions are based upon widely accepted philosophies, particularly when tied to the concept of a minimum standard of living. If other doctrines of social or economic worth are used, ability to pay may support tax systems proportional or regressive in nature.³

Richard Musgrave has noted that the "ability to pay" and the "benefits received" schools of thought have both had advocates of high and low public expenditures and advocates and opponents to progressive taxation. He indicates that the major distinction between these two philosophies does not lie in the level of governmental expenditure or in arguments of progressive versus regressive taxation. The difference is rather that the benefit theory emphasizes a relationship of exchange between taxpayer and government, while in the ability-to-pay approach the proper role of government in providing public services is viewed as a problem separate from the system of taxes, which are considered as compulsory payments.⁴

It is not the purpose of this study to justify or refute such theories, but rather to indicate their use when appropriate as arguments for or against particular taxes or tax systems. The fact that claims of regressivity, proportionality, or progressivity are not always supportable by objective measures does not blunt the emotional impact which is frequently an important factor in the adoption or rejection of particular taxes.

Economic Impact

In questions of equity and incidence, the individual taxpayer is normally the primary concern, though the taxpayer in this

³ See William J. Shultz and C. Lowell Harris, *American Public Finances*, p. 180-188, for a more detailed analysis of such theories.

⁴ Richard A. Musgrave, *The Theory of Public Finances*, chapters 4 and 5, particularly p. 61-63.

sense may be a corporation. Economic impact involves the broader effect of taxes on the community by encouraging, discouraging, or destroying segments of its economic life. Each individual is concerned with the amount of taxes he has to pay and understandably alarmed if his means of economic livelihood is threatened. (The pocketbook nerve is one of the most sensitive outside the human body.)

Because of the sensitivity to economic issues, the ways in which a particular tax may affect the business and economic life of the community becomes subject to extensive interest and speculation. Since almost every tax affects the business community in some way, either directly or indirectly, the facts as well as some fiction relative to the impact are likely to be disseminated widely.

One of the most difficult tasks is to properly assess the true impact of the tax program on the attitude of industry toward locating in a particular place or leaving another.⁵ The choice that industry makes is obviously influenced by a number of factors in addition to taxes. As a matter of fact, most studies have shown taxation to be of relatively minor concern in the location process. Questions of market, labor supply, site, water and raw materials, and transportation are of greater significance in the final profit picture than State and local taxes. Federal taxes are, of course, uniform and would not be a locational factor inside the United States.

Federal taxes affect the influence of State and local taxes on business in two ways. In the first instance they are generally so much larger than the State and local taxes that the latter seem less significant by comparison. Secondly, since State and local taxes are deductible from the Federal taxes they are reduced in fact. Any very large concern is probably paying the full 52-percent rate of the Federal corporate income tax, and that portion of the State and local taxes is, therefore, carried by the credit on the Federal tax. Whatever the level of State and local taxes, they are in effect halved by this process.

There is even a reverse twist to the problem of tax level. Some businesses profess concern for the overall community and feel that a community that provides adequate services is more likely to be attractive to higher caliber employees. Low taxes frequently mean inadequate services, and such businesses are willing to pay their share of the governmental costs.

If there are any firm conclusions to be drawn relative to taxa-

⁵ For an analysis of studies of tax influence on the location of industry, see John F. Due, "Studies of State-Local Tax Influences on Location of Industry," p. 163-173.

tion and the attraction of business and industry, they might be stated as follows. The community should not appear hostile to business in tax terms. Even those businesses that desire to pay their share of government costs do not appreciate discriminatory taxation or a system which may fluctuate widely, thus affecting cost calculations. Certain types of taxes work a special hardship on a particular type of business. Such effects should be weighed by the community at the time of adoption. Finally, the tax program of a local unit, unless very extreme, is likely to play only a residual role in the locational decisions of business. Only if all other factors are equal (a rare occurrence) is the decision likely to be influenced by the differences in tax programs.

Certain types of business may not be free to move, whatever the tax program. This may be true, for example, of retail establishments, which are generally tied closely to a geographical market area. Such businesses may be hurt by a decline in activity as a result of unwise taxation, and this in turn may have a serious economic effect on the community.* Self interest will usually prevent such drastically unwise decisions.

In summary, while the tax program of the local unit is unlikely to have serious economic impact unless it varies extensively from the norm, the possible and probable effects of new taxes on the economic base of the community should be considered in each case. The difficult task will be to separate the emotional arguments of those who *think* they will be hurt from the facts of economic impact.

Using the criteria above, one can now examine the major groupings of taxes utilized by local governments in the United States for the purpose of determining the possibility of applying presently available nonproperty taxes to school district use.

*See Robert A. Sigafos, "Economic Aspects of Local Nonproperty Taxes on Business."

CHAPTER 5

Per Capita or Poll Taxes

ALTHOUGH IT is the most widely adopted nonproperty tax used by school districts, the poll or per capita tax produces relatively small amounts of money under present practices. In addition to school districts, States and other local units may also be empowered to utilize this tax form. It was estimated in 1955 that the per capita tax could be used by municipalities in 34 States but that the use of this tax was declining. Municipalities in only 11 States were using the tax at that time.¹ Ten States were using the tax at the State level in 1960² as well as school districts in 7 States.³

Per capita taxes are historically old taxes and involve a flat rate applied to each person or a selected population group on the basis of age or sex, or both. Normally the rates have been low and, while the tax was originally designed as a revenue producer, it has fallen into some disrepute because of its tie with the privilege of voting in a few States. The concern of this study will be with the tax as a revenue producer.

Potential Yield

While per capita taxes produce only relatively small amounts in most States,⁴ they are capable of producing substantial amounts. The reason for this small yield in most areas is that the rate of tax is low, usually \$1 or \$2, and the enforcement of the tax is lax. In those States where the rates have been increased substantially and enforcement is attempted, the yields have increased to worthwhile amounts. In Pennsylvania, where the per capita tax may reach \$15 (\$5 under the school code, plus \$10

¹ Municipal Finance Officers Association, *Municipal Nonproperty Taxes*, p. 23. This is the latest available detailed survey of municipal nonproperty taxes.

² U.S. Bureau of the Census, *Compendium of State Government Finances in 1960*, p. 12.

³ See page 24 above.

⁴ An average of only \$0.83 per capita for municipalities over 10,000 population in 1955 and a total of only \$9,556,000 for all State governments in 1960. See footnote citations 1 and 2 above.

under Act 481), school districts in 1958-59 received \$29,840,252 from this source, or an average of .9 mills on the true market value of property in that State.⁵ In Vermont, where the per capita rates are equal to the property rate per hundred dollars plus the \$5 State old-age poll, the total per capita rate is frequently higher than in Pennsylvania and the yield substantial; but no separate figures on totals are available on a statewide basis.

School districts in Delaware also use the per capita tax extensively. Of the 45 local districts⁶ using local taxes in 1958, 29 levied a per capita tax in addition to the property tax. This tax ranged in rate from \$1 to \$8 and produced yields ranging from \$2.03 to \$22.28 per pupil. The per capita tax in Delaware also may be used for debt service or current expense or both with definite portions allotted for each.⁷

In determining the potential yield of this tax, one should know what the base is going to be. In Vermont the per capita or poll tax applies to all inhabitants over 21 and under 70 years of age, while in Nebraska, the permissive poll tax authority granted towns and cities extends only to male inhabitants over 21 and under 50 years of age. Even assuming the same rate and population in these two cases, one can see that the yield of one might run about three times the yield of the other. The range in the bases currently in use extends from all able-bodied males between 21 years and 45 years in Montana to all persons over 21 years of age in North Carolina.⁸

The yield of the per capita tax is perhaps the easiest of any to calculate. Once the base⁹ is set on the determinations of equity appropriate to the community, it becomes possible to estimate the population included in the base using Bureau of the Census statistics modified to take into account variations of school district boundaries from standard census tracts. In rapidly growing or declining areas or if the estimates are being made near the end of the census decade, problems may arise unless a special census can be conducted or revised population figures for the area are available.

Having estimated the theoretical yield which this tax can produce, one can then estimate the administrative costs and degree of evasion.

⁵ Governor's Committee on Education, *Facts and Figures on Education in Pennsylvania, 1958-59*, p. 101.

⁶ Using the State definition of district and not the Bureau of the Census definition.

⁷ John G. Farrea, *Local Taxation Summary, 1958*, p. 3.

⁸ Permissive tax for towns and cities in North Carolina. Commerce Clearing House, *State Tax Guide*.

⁹ Age range and sex.

Administrative Feasibility

Complaints about the problems of enforcing the per capita or poll tax are widespread. Under certain conditions, particularly urban areas with a highly mobile population, enforcement of the tax becomes difficult because it is hard or expensive to locate the taxpayer.* When the tax is small, it does not prove economically feasible to spend large amounts on enforcement, since enforcement costs could easily exceed the yield.

Historically in the United States, this tax has been made a requirement for the exercise of a highly desirable privilege, most commonly voting. If a person wanted to vote, then he would have to pay his poll tax as a prerequisite. The tax would be enforced automatically. At least two difficulties have arisen in the use of this technique. In many cases the problem has been to encourage persons to vote and the smallest inconvenience, such as the payment of a poll tax, may result in a reduction of turnout. Secondly, the poll tax has been used in many places to discourage voting and it then loses its significance as a revenue producer. In either case the effect is undesirable. As a result, the poll tax has been abolished in all but a few States, North and South, as a requirement for voting.¹⁰

The key to successful administration of the poll tax is apparently found in the ability to find an adequate penalty for violation. The most effective device to come to the author's attention is the provision in Vermont which allows the denial of a driver's or motor vehicle license if the nonpayment of the poll tax is reported to the State. This device strikes at a privilege which is not only desirable but to many people also essential. While no one would deny that voting is the most valuable privilege which citizens in a democracy possess, experience has shown that in the United States it is a privilege which is appreciated in the breach. Less substantive but more widely used privileges therefore become a better basis for per capita or other tax enforcement. It should be noted, in passing, that Vermont also denies voting privileges in State and local elections for nonpayment of poll taxes, but it is the other enforcement which is considered more effective.

¹⁰ Only five States in 1962 required a poll tax for voting in all elections including those for Federal offices. At least one additional State may deny the voting privilege for State and local elections in the event of nonpayment of the poll tax. An amendment to the Constitution is currently before the State legislatures which would prohibit the requirement of a poll tax payment for voting in Federal elections.

In addition to these techniques of enforcement, Vermont has a higher poll tax than generally used elsewhere and the only one which varies from year to year. The poll tax in Vermont is composed of a State flat-rate levy plus a local levy which is equivalent to the ad valorem property tax rate per \$100 of assessed valuation for all local functions. These rates are quite substantial and the poll tax can produce significant sums.¹¹ The yield of the poll tax is divided among the various functions, e.g., schools, fire, or municipal, on the basis of their portion of the total property tax rate. The State poll tax is earmarked for old-age assistance.

Compliance ratios vary extensively but are difficult to document without considerable research. Estimates indicate a range running from very low to as high as 95 percent or more.¹² The latter ratios would compare favorably to almost any tax compliance. In most cases, however, the compliance would seem to be extremely low. In some it is so unsatisfactory that officials have indicated that they would prefer to abandon the tax. Since it does produce some revenue, however, there is a reluctance to abandon the income without a substitute or replacement, particularly where budgets are tight, an almost universal situation.

Good estimates of the administrative costs of the per capita tax are difficult to obtain, basically because this tax in most instances does not require separate administration. It may be payable along with other taxes. The major expense would be in compiling a list of persons subject to the tax and conducting a periodic review for current applicability. Other costs would be for the mailing of notices, recording of payment and followup or enforcement. Since the rate is flat there are no auditing costs to insure proper reporting. Compliance costs will be in inverse ratio to the acceptance of the community and a willingness to enforce. The fractional nature of the manpower needs involved in the administration of the per capita tax in any but the largest districts virtually requires its being handled in conjunction with another tax so that its administrative costs become of little consequence, particularly if the rate of the tax is reasonably high. To be somewhat arbitrary, it would seem that any rate below \$5 under present conditions is only useful for other than revenue purposes, if administrative costs are to be kept at a reasonable percentage of the yield.

¹¹ Poll taxes for Middlebury, Vermont, in 1960, for example, totaled \$17.76 per person.

¹² Interviews on a selective basis. In addition, per capita yields as low as \$0.06 in some municipalities, while somewhat misleading when removed from the context of levy and range of application, would indicate a low level of compliance. See Municipal Finance Officers Association, *Municipal Nonproperty Taxes*, p. 28.

Conclusions

The administrative experience in most school districts and other local units would be rated unfavorable with respect to the per capita or poll tax. It has proven satisfactory in Delaware, Vermont, and some districts in Pennsylvania. All of these States utilize a high rate. The fact that it has proven satisfactory in a few places would indicate that it is possible to administer such a tax if it can be made acceptable philosophically and psychologically to the taxpayers and the governing body so that there is a willingness both to enforce and to comply with the tax. Experience would seem to support the proposition, however, that this tax is more adaptable to small units of government¹³ than to the highly mobile larger communities. In addition, more satisfactory results are likely to occur in balancing yield with administrative costs if the tax is kept above \$5 per capita.

Equity and Incidence

The incidence of a per capita tax is perhaps one of the easiest to trace. It is a personal tax and falls directly upon the individual who pays the tax. While a varying portion of this tax will be credited against the Federal and possibly State income tax, depending upon the bracket of income of each payee, this is not a feature peculiar to the per capita tax but applies to any local tax. This illustrates that in no case is incidence clearly measurable, but in the per capita tax, it is clearer than most. There is essentially no way to pass on the major impact of the tax, thus it will rest as fully as any local tax upon the residents of the community which impose it.

Whether or not the per capita tax is equitable poses a knottier problem. The arguments pro and con can be boiled down to a few major points, but the choice may not be made much easier. Objections to the per capita tax are usually based upon the fact that it is not related to ability to pay or a measurable benefit.

Proponents of the tax may cite the advantages of having everyone pay some tax on a minimum basis. This may be justified on the grounds that everyone receives government benefits and a portion of the income is appropriate to defer these costs.¹⁴ This may be particularly true with respect to education which is so

¹³ One statement with respect to this tax is that "administrative problems would appear to increase with the size of the community." See Municipal Finance Officers Association, *Ibid.*, p. 29.

¹⁴ See William J. Schultz and C. Lowell Harris, *American Public Finance*, p. 239.

broadly based in this country. It has also been noted by others that the per capita or poll tax may tap those who rent and those who neither rent nor own property and, therefore, escape the property tax.¹⁵ The latter group would be relatively small unless family dependents are categorized as nontaxpayers, and renters do pay property taxes indirectly.

While no real attempt is made to relate the per capita tax to ability to pay, there are generally some limitations from the viewpoint of equity designed to exempt groups likely to have no income or reduced income. For example, the placing of age limits from 21 to 60 would exclude most of those too young to work and many retired persons. An age range of 18 to 65 might represent the broadest base which could be justified on these grounds. In addition, women have been exempted; but with the growing proportion of the work force being made up of women, exemption on grounds of probable nonemployment would seem to have less validity. Military personnel, because of their transient situation, are frequently exempted. Many States also exclude the blind, deaf, paupers, disabled persons, and the insane from these taxes.

The range of coverage is an important element of equity in relation to this tax and should be as broad as possible in order to achieve an adequate yield. The fewer the exemptions or exclusions, the easier the administration of the per capita tax. Since it is impossible to make a per capita tax fully equitable according to principles of ability to pay or government benefit, the exclusions or exemptions should only be used to remove the most objectionable features of the tax. If the range of coverage is too narrow on an age or sex basis, the resultant discriminatory features will further affect the equity of the tax.

Economic Impact

Since there is virtually no way in which the per capita tax can affect a particular business, considerations of economic impact are negligible or nonexistent in this case. Every tax has an economic impact on the individual or business which pays the tax, but of primary concern is the impact which is discriminatory or has a general, depressing economic effect. Neither of these conditions would normally result in the per capita tax unless the rates were extremely high, or the range of coverage extremely limited, or both, situations which have not occurred in practice. A per capita tax of \$200 for each individual between the ages of

¹⁵ Arvid J. Burke, Mabel Walker, and Anne Phinney, "Local Nonproperty Taxes," p. 113.

21 and 40, for example, might make it extremely difficult for a community to attract or keep prime working groups or the businesses that hire them. It is only this type of theoretical extreme which could have serious impact, and there is no indication that such an application would occur in practice.

Summary

While the per capita or poll tax is one of the most widely used nonproperty taxes at the local level, its total yield for local purposes falls at the bottom of such taxes.¹⁸ For school purposes this tax is more significant, primarily due to its heavy use in the State of Pennsylvania.

The per capita tax is frequently resisted on grounds of inequity and the ineffective administration which is found in most States. Good examples do exist, however, that seem to show that it can be properly and efficiently administered, if desired.

A major advantage which this tax holds for school districts is that it can be administered by any size district from the smallest to the largest. It tends to be less effective in the larger districts, however, and thus is particularly adaptable to the small and medium range districts, in fact the most adaptable of all nonproperty taxes to such districts. If the rates are set sufficiently high and the range of coverage broad, the yields can be substantial, a factor which should enhance its consideration.

¹⁸ Municipal Finance Officers Association, *Municipal Nonproperty Taxes*, table 3, p. 8.

CHAPTER 6

Income Taxes

MORE REVENUE for any given percentage rate is produced by the income tax at the local level than by any other nonproperty tax.¹ This is true because the income tax used at the local level in the United States is a flat rate tax on a broad base with very few exemptions and deductions. Its close competitor, the sales tax, normally uses a more restrictive base and thus must rely on higher average rates to produce the same yield. In 1961, approximately 103 cities and villages, 240 boroughs, 40 townships, and 800 school districts were using local income taxes in 5 States.² All but 73 cities and villages of this group of local units were located in the State of Pennsylvania. Detroit, Michigan, used its home rule powers in 1962 to adopt a 1-percent income tax which was put into effect after the State legislature approved a bill banning such taxes and the governor vetoed the legislative act.

Only in Pennsylvania have school districts used the local income tax. The districts in that State have shown an increasing propensity to adopt this source of revenue, and the number using the income tax has risen from 456 in 1957-58 to 599 in 1958-59 to the 800 cited above.³

Types of Income Taxes

If all varieties of income taxes were considered as available for possible school district use, they would add up to a substantial number. They may be grouped into categories of gross income or net income, flat rate or progressive, and types of income included, such as wages and salaries, business profits or investment income, or various combinations of these categories.

In actual practice the income taxes at the local level have all

¹ Municipal Finance Officers Association, *Municipal Nonproperty Taxes*, 1958, p. 25.

² Advisory Commission on Intergovernmental Relations, *Local Nonproperty Taxes and the Coordinating Role of the State*, p. 38. The States were Alabama, Kentucky, Missouri, Ohio, and Pennsylvania.

³ David F. Stafford, *Financing Education in Pennsylvania*, p. 2.

been flat-rate taxes and in all cases are imposed on salaries or wages and unincorporated business earnings. Outside of Michigan they do not apply to investment income. Except for Pennsylvania, corporate net earnings are taxed, but probably because of the flat rate, do not generally provide over 20 percent of the total local income tax revenue. Because they are restricted largely to salaries and wages, these taxes are frequently referred to as wage or payroll taxes. While it is true that only New York City at the local level is authorized to levy a formally named "payroll tax" * (one half to be paid by the employee and one half by the employer) and that this tax has never been imposed,¹ the bulk of local income taxes comes from wages, particularly through withholding, and it is therefore not unreasonable to use the term wage or payroll.

Potential Yield

The local income or earnings tax, as indicated above, is perhaps the greatest potential revenue producer of any nonproperty source at the local level, particularly under urban conditions. In 1960, 5 out of the 6 largest cities in the United States obtaining over 50 percent of their taxes from nonproperty sources were using the local income tax.² The sixth was using a general sales tax. Although the income tax does not produce enough revenue for all local governments to justify Bureau of the Census annual tabulations, except for the largest cities, the 1957 *Census of Governments* showed almost \$191 million collected from this source for all local governments.³ This amounted to only \$1.12 per capita or about 1.3 percent of all local taxes.⁴ In 1960, however, the 43 largest cities collected approximately \$174 million from income taxes.⁵ This amounted to \$4.66 per capita.

Per Capita Yields

For those eight cities using the tax, the per capita figure of \$30.02 becomes significant. Even omitting Washington, D.C.,

* The Federal Old Age and Survivors' (Social Security) Tax is a payroll tax.

¹ The city by municipal ordinance in 1934 authorized the levy of a local income tax based on a percentage of the Federal income tax but repealed the ordinance before the tax became effective. The "payroll" tax authorized by the State legislature has never been applied. See Robert A. Sigafos, *The Municipal Income Tax: Its History and Problems*, p. 3-4.

² Advisory Commission on Intergovernmental Relations, *Local Nonproperty Taxes and the Coordinating Role of the State*, p. 29-30. Excludes Washington, D.C., which also uses income tax from the 50 largest cities.

³ U.S. Bureau of the Census, *U.S. Census of Governments: 1957*, Vol. III, No. 3, *Compendium of Government Finances*, p. 178.

⁴ U.S. Bureau of the Census, *ibid.*, p. 24.

⁵ U.S. Bureau of the Census, *Compendium of City Government Finances in 1960*, p. 66. Population figures on p. 9.

from the figures, because its tax more nearly resembles a State tax, leaves a per capita figure of \$27.51. The income tax in the 7 largest cities using this tax, listed below, amounts to 36.3 percent of all taxes collected and 75.0 percent of the property tax. It can be seen from these figures that where the income tax is used it approaches the property tax in value. The property tax in these same cities provides 48.4 percent of the total tax revenue, which is less than the average for all cities.

In 1955, a survey of municipalities over 10,000 population showed that 48 were using an income tax with rates ranging from 0.125 percent to 1.25 percent at an average per capita yield of \$16.25. At a given rate the average per capita yield tended to be larger for the larger communities. The average per capita yield on the actual rate ranged from a high of \$23.57 down to \$2.90.¹⁰ The highest per capita yield, then as now, was obtained in Philadelphia, which also used the highest rate and broadest base.¹¹ Philadelphia's per capita yield has gone from \$23.37 in 1955 to \$35.41 in 1960.

The per capita yield for local income taxes of other cities or local units can be used as a basis for estimating the potential yield to a school district if the same type of tax is used and the economic makeup of the two communities is similar. An indication of the variation which can occur, however, is illustrated by the following list of per capita yields in 1960 adjusted to a 1-percent rate for cities over 300,000 population that impose a local income tax: ¹²

City	Per capita yield in 1960
Philadelphia -----	\$23.61
St. Louis -----	19.77
Pittsburgh -----	17.06
Cincinnati -----	31.53
Columbus -----	26.57
Louisville -----	22.10
Toledo -----	27.17

Contributions of Nonresidents

One of the key factors in determining the yield of a local income tax is the relationship of the nonresident to the tax. A major argument for adopting such taxes has been the possibility

¹⁰ Municipal Finance Officers Association, *Municipal Nonproperty Taxes*, p. 34.

¹¹ Philadelphia is able to tax nonresidents and now applies a rate of 1.625 percent. Only Newport, Kentucky, and Gadsden, Alabama, have higher rates at 2 percent.

¹² Yields taken from U.S. Bureau of Census, *Compendium of City Government Finances in 1960*, tables 5 and 7.

of taxing the income of nonresidents who work in the taxing jurisdiction. Philadelphia's tax does tap nonresident income, and many subsequent adoptions outside of Pennsylvania have followed this same pattern. Without arguing the question of the equity of such a tax at this point, it must be emphasized that those tax jurisdictions which are able to tax nonresidents will have a greater per capita yield than those which cannot. Except for Pennsylvania, exclusive of Philadelphia, where residence is given legal priority and a few Ohio cities which allow reciprocity, nonresident income is tapped. In Kentucky, since the income tax is actually an occupation license, residents who work outside the taxing jurisdiction are not taxed. This reduces the per capita yield.

Estimates of the percentage of tax from nonresidents were made in 1954 for selected cities.¹³ The percentages for some of the larger cities were:

City	Percentage of tax from nonresidents
Philadelphia -----	15.0
St. Louis -----	25.0
Pittsburgh -----	10.0
Cincinnati -----	17.0

For other smaller cities the range was from 2 to 65 percent. The extremes can be accounted for by the legal status of nonresident taxation and the peculiar nature of the employment pattern. It is quite likely that the nonresident contributions of the cities listed above have increased in recent years as higher paid employees have moved to the suburbs. Estimates for St. Louis now range from 30 to 35 percent and a similar increase could well occur in other areas.¹⁴

These matters must be taken into account in any evaluation of the potential of a particular jurisdiction to produce earnings tax revenue. The taxing jurisdiction that is able to tax both resident and nonresident is in the strongest position, but it would be expected that, if a large number of taxing jurisdictions within a State are permitted to use this source of revenue, some reciprocity or priority arrangement would ultimately be established thus reducing the potential yield for any single jurisdiction.

Administrative Feasibility

While there is little question of the potential yield of the income tax, there are some administrative problems which can affect the

¹³ Robert A. Sigafos, *The Municipal Income Tax: Its History and Problems*, p. 79.

¹⁴ Detroit with its newly adopted wage tax expects that approximately 25 percent of the tax paid by individuals and 20 percent of its total tax will come from nonresidents. Based on estimates given in Leonard D. Bronder, "Michigan's First Local Income Tax," p. 427.

net yield of the tax and need to be carefully considered. There has, however, been adequate experience with the income tax at all levels of government to provide possible solutions to many of the problems if there is a sincere desire to correct them. The Federal Government has been active in income taxation since 1913; the States, beginning with Wisconsin, from 1911;¹⁵ and local governments, beginning with Philadelphia, from 1940.¹⁶

Since the income tax is basically a self-assessed tax, compliance problems can arise. One of the most significant administrative developments in the income tax field was the introduction of the withholding system. This device is particularly significant at the local level where the bulk of income subject to tax is derived from wages and salaries. The withholding device makes the wage or earnings tax feasible in much smaller jurisdictions than would be the case otherwise. The employer becomes the enforcer of the tax and while the administrative costs of such a procedure can be substantial, particularly where the employer must withhold for a number of different jurisdictions, the administrative cost to the local unit is considerably reduced, unless an allowance is made to the employer for such service.

Administrative Costs

Administrative costs for local nonproperty taxes are difficult to determine, particularly for smaller jurisdictions, since the administration of the nonproperty tax may be placed under an existing tax unit. Some estimates of the costs of collection have been made, however, and generally range between 2 and 5 percent of gross yield, with some approaching 10 percent and a few under 2 percent.¹⁷

The wide variation in collection costs can be explained on grounds other than efficiency in administration. There is a certain minimum of staff required to administer a tax, and this minimum may serve a fairly wide range in number of taxpayers. The smaller unit is going to have a larger percentage cost than the larger unit within this range. Also since it does not cost any more to levy a tax of a high rate than a low rate, the low rate community will as a result have a higher percentage collection cost.¹⁸ Further, a community with large payroll industry and

¹⁵ For a brief history of State income taxation, see Clara Penniman and Walter W. Heller, *State Income Tax Administration*, p. 2-8.

¹⁶ Dates of continuous use of the tax.

¹⁷ Robert A. Sigafos, *The Municipal Income Tax: Its History and Problems*, p. 59-64.

¹⁸ Exceptionally high rates may increase enforcement costs, but even here the added revenue might dwarf the added costs by comparison.

high percentage of its total return based on withholding will be able to obtain a high yield with relatively little enforcement or additional administrative costs for such enforcement.

Employers' discount.—If an employer's discount to compensate for withholding costs is involved, such as is used in St. Louis, this must be added to the costs of collection. There the city's administration costs are running only slightly over 1 percent, but when the 3 percent discount is added, the total administrative costs are in excess of 4 percent.¹⁹ On the surface, discounts to employers might seem to be equitable but there are difficulties and reasons for not adopting such practices. In the first place, all of the employers affected by a local earnings tax would already have procedures established for withholding for Federal income and social security taxes and, in some cases, State income taxes. While the addition of another deduction might add some burden of cost, it is likely to be quite small except where payments to multiple jurisdictions, such as in Pennsylvania, occur. Even if the costs are significant, there is no single amount of discount which would be adequate or fair for all employers. To some large employers where a machine tabulation system has already been established, the very substantial amounts which can derive from a large payroll might be more than adequate, while in a smaller business where the added burden might require the addition of machines or hiring another person, the amount might be entirely inadequate. Finally, and not unrelated to equity, most governmental jurisdictions do not allow discounts for employer withholding but assume that this is simply an additional cost of doing business, the impact variations of which cannot be changed by a flat rate discount. If looked at as a tax, then it can be considered a variable business tax. Any jurisdiction, therefore, that adopts such a provision does little except to reduce its potential yield.

Degree of enforcement.—The degree of enforcement can sharply affect administrative costs. With approximately 80 percent, on the average, of earnings taxes being collected by withholding, there may be some temptation for the local units to be rather lax about enforcement in other areas of income. Enforcement in the form of auditing of employers' accounts would be necessary even if all the money came through withholding. With the number of employer accounts averaging about 25,000 per 1,000,000 population among the larger cities, this alone can pose a

¹⁹ This discount has been reduced to 1.5 percent effective November 1, 1961.

sizable problem.²⁰ While a high percentage of the total employees may be narrowed down to a much smaller number of employers in most areas, it is still necessary to do considerable auditing, even though complete auditing of all would probably be impractical. If returns are required from both employees and employers as in most jurisdictions, some office auditing and correlations can be made, particularly with punch card systems. If individual returns are not required unless income not subject to withholding is involved, then field audits become a necessity.

Employment Outside Taxing Jurisdiction

Perhaps the most difficult aspect of enforcement involves residents of a taxing jurisdiction who work outside of that jurisdiction. It is sometimes difficult to get the cooperation of employers outside to supply information useful to the taxing unit. Federal agencies, in the past, have presented some problems since they do not withhold for local units and have not always been cooperative in supplying information to these units. The pattern of cooperation has improved so that problems should not be as severe today. The existence of a large Federal installation, even within the boundaries of the taxing jurisdiction, will require additional enforcement expenditures, however, because of the absence of withholding and the requirement of individual filing and payment by each Federal employee.²¹ There are various techniques which can be used to ferret out the resident who is employed outside the taxing jurisdiction, but of primary importance is a desire to do the job and a willingness to employ sufficient staff to make the necessary checks and audits. There has been some reluctance on the part of legislative bodies to provide the necessary staff for proper enforcement of the income tax at all levels, even though it can be shown that additional collectors can more than pay for the extra cost with increased revenue return. The traditional apprehension toward tax collectors and fear of possible tax harassment remain.

Size of Jurisdiction

There may be some implication that smaller jurisdictions are less able to administer successfully the local income tax than

²⁰ Derived from Robert A. Sigafos, *The Municipal Income Tax: Its History and Problems*, p. 41, table VI.

²¹ St. Louis attributes a large portion of its administrative cost to enforcement against Federal employees, of which there are about 25,000 in the St. Louis Metropolitan area. St. Louis does not require returns from individuals whose earnings are subject to withholding.—Statement of John H. Poelker, Comptroller, dated October 28, 1959.

larger jurisdictions, particularly when it is noted that the larger jurisdictions generally obtain larger per capita yields from this tax than the smaller communities. As noted above, however, per capita yield may be more related to the nature of the tax base than to the administrative efficiency of the unit.

Robert A. Sigafoos points out that based on his experience "... derived from visiting and canvassing more than 100 separate communities in Pennsylvania, Ohio, Kentucky, and also St. Louis, Missouri . . ." ²² there does not appear to be any relationship between size and efficient or effective collection. He does not feel that even the presence of a dominant industry to ease administration through the withholding function is necessary for efficient administration. He has expressed the view that in the matter of effective collection the larger communities have not shown themselves to be either better or worse than the smaller. The tax collectors' intimate knowledge of the financial affairs of the local citizenry in the small community may actually offer an advantage over the impersonality of the large jurisdiction's administration.

Without question, a taxing jurisdiction can be too small to administer effectively a local income tax. Frederick D. Stocker does not feel that the earned income tax can be effectively applied to farm income, ²³ and the Committee on Educational Finance of the National Education Association has noted that "many school districts in the United States are too small to administer even the property tax." ²⁴ Cooperative arrangements among the smaller jurisdictions can overcome to some extent even this objection, and these arrangements have been utilized in several Pennsylvania areas.

Equity and Incidence

Taxation of income is considered by many if not most economists to be the most equitable form of taxation. This, of course, assumes certain criteria in the way that income is taxed. One author in support of the income tax has said:

... The income tax is not a tax upon income but a tax upon persons according to their respective incomes; and, subject to the requirement of adherence to simple, general rules, the objective of policy must be fairness among persons, not fairness among kinds of receipts (whatever that might be construed to mean). . . . ²⁵

²² Robert A. Sigafoos, *The Municipal Income Tax: Its History and Problems*, p. 65.

²³ Frederick D. Stocker, *Nonproperty Taxes as Sources of Local Revenue*, p. 59.

²⁴ National Education Association, Committee on Educational Finance, *New Local Sources of Tax Revenues*, p. 20. Administration is handled by some other unit of government.

²⁵ Henry C. Simons, *Personal Income Taxation*, p. 128.

The way in which such a tax should be levied also becomes a part of the total scheme. This same author further states:

... The personal income tax should be progressive; it should be levied according to simple general rules or principles (complexity in detailed application is, of course, unavoidable); and, subject to this latter requirement, it should be as equitable as possible among individuals. Thus, it must proceed from a clear and workable conception of personal income; and it must be constructed in such manner as to minimize the possibilities, both of lawful avoidance (defined in terms of the basic conception of income) and of successful evasion through false declarations. . . .²²

The conception of income in this case is defined in broad inclusive terms so that the income tax becomes the modern "single tax." Virtually all existing exemptions would be removed and with the income base broadened most existing excise taxes, tariffs, and license taxes, except those needed for regulatory purposes, would be abolished. This approach is based upon the assumption that all taxes ultimately come from income and that, therefore, the most desirable approach is to go to the primary source. The real problems arise in determining what categories of monetary and nonmonetary income should be included. The ultimate goal of a true personal income system would be to assess accurately the *net* worth (taking into account gains and losses) of each individual at regular intervals and to tax the positive change in net worth. Our present approach to this concept using inclusions, exclusions, and exemptions by particular categories of income is certainly imperfect in its results, and much of the discussion on both theoretical and "practical" levels is concerned with the total impact on the individual. This becomes extremely difficult to evaluate when all of the interrelationships and complexities are taken into account.

Progressive Taxation

Interwoven with the concept of total net income is the concept of ability to pay and the marginal utility of money, which leads many persons to emphasize progressive taxation. The assumption of most supporters of the income tax is that the larger the net income, the greater the proportion of it which should be taxed. Stated simply, progressive taxation is equated with ability to pay and closely if not completely with the broad concept of equity. The degree of progression which should be adopted is not easily

²² Ibid., p. 206.

settled even if it is agreed that progressive rather than proportional or regressive rates should be used. Should all income above a certain level be taken or should the maximum rate be 95 percent, 65 percent, 45 percent, 25 percent or any other? While maximum rates are ultimately adopted and even changed, there is really very little objective basis on which to determine the maximum or step rates. To a high degree these are determined by the test of political acceptability and need for revenue. The true impact of the rates of progression are further clouded by the effect of exemptions, deductions, and special treatment of different categories of income. We know, for example, from Treasury Department statistics that very few persons in the United States pay over 50 percent of their income in taxes in spite of a maximum step rate of 91 percent for income over \$200,000, \$300,000, or \$400,000 depending on marital status, and a maximum average rate of 85 percent. Proposals to reduce the maximum rates have been and are supported, if not on equity grounds, on the basis that the reduction in governmental income will be slight and could be overcome completely with modifications in the exemptions. This raises additional questions of equity, however.

Progressive rates are frequently examined on the basis of their impact on the availability of investment capital. There is no question but that the rate structure of the income tax can modify the distribution of income and that considerations of the direction which modifications should take are important. These considerations, once again, become highly complex, bring disagreement among economists²⁷ and should involve a degree of experimentation. Such experimentation is difficult to obtain, however, because of the political pressures and maneuvers involved and the resulting extremely slow process of getting rate structure changed. The changes are wrought more frequently by crises than in any other way.

From the foregoing discussion it can be seen that the income tax in its full conception would be neither easy to adopt nor easy to apply on an equitable basis. At the local level in the United States no income tax has been adopted which either (1) covers all income or (2) uses a progressive rate.²⁸ The local income tax is then more nearly a tax on special categories of income than it is a tax on income *per se*.

²⁷ Social goals may be as important as economic goals in supporting the concept of progression. See T. R. Beard, "Progressive Income Taxation, Income Redistribution, and the Consumption Function."

²⁸ Denver proposed a tax with a one step progression in 1955 but the tax was never put into effect.

Exempted Income

Since to many even a proportional income tax is inequitable, and on the basis of income taxed may actually be regressive, especially when large sources of income such as that from investments are omitted, it is not surprising that opposition to the use of local earnings taxes has developed. In its treatment of the municipal income tax, the American Federation of Labor and Congress of Industrial Organizations, after noting some of the advantages of this tax, states:

*... All of these advantages, however, are cancelled out by the glaring inadequacy of the existing municipal payroll taxes which so clearly violate the principle of ability to pay. The fact that these taxes allow no exemption for dependents and fail to tax all income whether from dividends and interest or any other source makes them more regressive in their impact on poorer families than even a local sales tax. . . .*²⁹

While the AFL-CIO goes on to indicate that if the tax base were broadened and certain exemptions provided,³⁰ the municipal income tax, even with the flat rate, would be less regressive than existing sales and property taxes, Henry C. Simons feels that the States, much less the local units, could never employ an equitable personal income tax. Only the Federal Government has the broad jurisdictional powers and integrated national administrative and enforcement machinery necessary for proper utilization of the true personal income tax, according to Simons.³¹

Ability To Pay

Equity, it should be obvious by this time, means different things to different people and there are probably no absolute standards which can be applied.

The "ability to pay" argument, for example, implies that it is desirable to tax the wealthy and spare the poor. This is a widely accepted argument for various reasons but is not as simple to apply as it might seem on the surface. The definitions of "poor" and "wealthy" become critical under this approach. Any effective tax system must actually tap the broad base of the population

²⁹ American Federation of Labor and Congress of Industrial Organizations, *State and Local Taxes. . . A Handbook on Problems and Solutions*, p. 95.

³⁰ Only three cities in Ohio now permit personal exemptions, and two of these are used only to eliminate small returns since the full tax applies to the total income if it exceeds the amount of exemption. Milton C. Taylor, "Local Income Taxes After Twenty-One Years," p. 115.

Detroit and Hamtramck, Michigan, provide \$600 exemptions in their income taxes adopted in 1962. Leonard D. Bronder, "Michigan's First Local Income Tax."

³¹ Henry C. Simons, *Personal Income Taxation*, p. 214-215. He would provide States relief by sharing the Federal tax with them.

because it is here where the productivity lies. Only a society which is extremely unequal to the point that all of the wealth lies in the hands of few could survive on taxes from the "wealthy" alone, at least in the traditional sense of the term "wealthy." Even here it will be the "poor" that pay in the final analysis through the denial of wealth and benefits.

A tax system can be used to break down inequalities in wealth by achieving a redistribution of that wealth in the form of governmental benefits to deprived groups paid for by taxes on the privileged groups.

In the United States a complete equalizing of wealth is not a goal of the tax system because we support the proposition that there should be relatively wide ranges of wealth allowed as an encouragement for greater productivity and entrepreneurial activity under a free enterprise system. Extremes of poverty and wealth, where they occur, do become matters of concern.

In our own relatively egalitarian society, it is the broad middle income group that bears the heavy tax burden. In 1960 over 60 percent of the Federal personal income tax was paid by persons earning incomes between \$5,000 and \$20,000. Thirty-nine percent of such taxes were paid by those earning between \$5,000 and \$10,000.²²

In a free society, further, many of the supposed inequities will actually adjust themselves through a process of capitalization or will be offset by nontax methods. As a matter of practice it becomes necessary to allow for some self-adjustment since it becomes almost impossible to anticipate the effect of many tax actions.

To illustrate how these adjustments may work, one can take the case of exempting or extending favorable treatment to certain types of income. To many this seems to be inequitable. On the other hand, the value of such exemptions tend to be capitalized into the income. The interest from State and local bonds is exempt from the Federal income tax, but the interest rates on these bonds tend to be lower because of the tax advantage. As a consequence, the loss to the Federal Government is offset to some degree in the entire economy in savings to the State and local governments. A tax on earnings, as a further example, could produce a demand for higher wages which would partially offset the tax. The increased wages might come at least partially from a reduction in profits which can be smaller because dividends are not taxed

²² U.S. Treasury Department, Internal Revenue Service, *Individual Income Tax Returns for 1960*, p. 82.

under an earnings tax. It is quite easy, of course, to point out that the compensations in these cases do not necessarily benefit the same persons who are injured. This is true, but the purpose of the illustration is to show that under our complex economy it is necessary to assume a certain amount of self-adjustment which will ultimately correct initial inequities.

It might further be pointed out that society may directly aid through various governmental or private welfare programs those who have been harshly or inequitably treated by the economic or tax system.

Tax Supplement

A dilemma is created by the comments on the establishment of an equitable local income tax thus far—if the tax is made equitable on the basis of ability to pay and extended coverage, it becomes difficult if not impossible to administer efficiently. There are two possible solutions to this dilemma. One would be to shift the administration of the tax to a higher level through the use of tax supplements and the other would be to redefine or to view in a different light the question of equity.

As to the former, there has been some experience in the Scandinavian countries with the tax supplement. In the United States, the sharing of the income tax with counties and municipalities in Maryland³³ and Wisconsin would be the nearest approach to the tax supplement.

To be considered as a true supplement, however, the use of the additional tax on the State rate should be optional at the discretion of the local unit. This is not true of the tax sharing devices presently used. To get real equity, even through the tax supplement, the State tax would have to meet equitable standards. It should be noted that Maryland uses a flat rate tax and, therefore, would not meet ordinary "ability to pay" criteria, though it does tax investment income at a higher rate than wage or salary income. There is, however, much merit in the tax supplement argument particularly if the State income tax system is accepted as reasonably equitable and if the local income tax were to be used widely in the State.³⁴

³³ Since Maryland schools are dependent, a portion of the county share can technically be described as going to the schools, but in practice is not generally so designated.

³⁴ Since there has been little inclination to go all the way to a comprehensive income tax system as advocated by Simons, cited above, equity arguments at the State and Federal levels have generally hinged around the progression of rates and exemptions and deductions. The tremendous growth of State financial activities in the past 25 years would probably indicate a potentiality for creating a more equitable system than was apparent in 1938.

Adjustment to the Tax System

With emphasis on the self-adjusting features of a tax system, there may be strong arguments for applying taxes without any exemptions or deductions and allowing the income levels to adjust to the tax situation. Direct governmental appropriations could be used to meet those needs of individuals and groups which are socially approved but not provided through private means and self-adjustment. This system would have the advantage of clarity, comprehensibility, and responsibility which is frequently missing from our present tax system of deductions, exemptions, and variable rates. The obvious roadblock to change in the direction of a simpler and clearer tax system is that the inequities and complexities of the present system have been *capitalized* into the economy and any rapid or major changes may bring about serious dislocations.

Emphasis needs to be made at this point that the author is not supporting a nihilistic tax system. The purpose of this discussion is to show that it may be acceptable to adopt a tax against which there are strong arguments of inequity, but which may be offset by certain other advantages. The earnings or local income tax may be objected to on equitable grounds because it is a flat rate and allows no exemptions. It is supported by many, however, because it taxes commuters, considered desirable, or because it prevents a rise in a tax considered even more inequitable, the property tax. Each person and community will, in effect, have to decide as to the justice or injustice of the tax.

Summary of Some Arguments on Equity

In order to help in this process, a number of the pro and con arguments are summarized below under some general points which are frequently emphasized.

Theoretical equitability.—This point has been discussed at length above, but to summarize, it is frequently argued that the local income tax is inequitable because it uses a flat rate, thus not recognizing "ability to pay," and because it does not cover all income, just wages and salaries, thus becoming regressive. This argument is countered by emphasizing that the local income tax is less regressive than the property tax already in use and which it is designed to supplement. It thus represents an improvement, and all that can be achieved by extending exemptions and progression is to make the tax difficult, if not impossible, to administer locally. The flat rate income tax like other proportional

or regressive taxes can also be considered as an offset to the highly progressive rates of the Federal income tax.

Size of base.—The fact that all income is not included is criticized on the grounds that it not only adds regressivity but also allows some persons to escape payment altogether. On the other hand, only a relatively small proportion of family units survive on investment income alone, the major exclusion, and more persons will contribute to this tax than any other except the sales tax.

Stability of tax base.—There are various arguments which can be made in this area. One of the big advantages of the local income tax is that it rises automatically along with salaries and payrolls without a change in rate. The property tax, on the other hand, is dependent upon reassessment and increased rates to take advantage of a growing or inflating economy, a process fraught with political difficulties and frequently slow. The reverse side of the coin, of course, gives a different picture. Income tax receipts also decline in a period of recession, while the property tax will hold fairly stable. A major depression is an event which no tax can adequately meet without serious adjustment, so it need not be considered for these purposes. With a business downturn or slight recession, the fixed taxes, e.g., property, will generally be met while the income tax would automatically decline. Some experience with the local income tax already indicates that certain communities suffered declines in income tax collections during the recessions of the 50's or under economic disturbances peculiar to their locale.³⁵ From the point of view of equity, however, it can be noted that the income tax applies only when there is income, while the property tax may cut into savings or capital.

Multiple taxation.—With the existence of Federal, State, and local income taxes, there is the possibility and actuality³⁶ that the same income can be taxed three different times. If more than one overlapping local unit³⁷ were allowed to use the tax, as in Pennsylvania, the pyramiding could exceed three. By establishing some theoretical rates, it may be shown that this income could be taxed at over 100 percent. Such a situation would be indefensible and has never occurred. Under present laws, deduction of State and local income taxes are allowed in Federal income tax calculations, and occasionally, Federal income taxes may be deducted from State income taxes. Local income taxes presently allow no such deductions.

³⁵ Robert A. Sigafos, *The Municipal Income Tax: Its History and Problems*, p. 123-124.

³⁶ For example, in Alabama, Kentucky, and Missouri.

³⁷ For example, municipalities and school districts.

The annoyance factor of such multiple taxation is more likely to present a problem than the question of equitability, though the adoption of a local income tax would have to consider the existence of the Federal and possibly a State income tax. Widespread adoption of the local income tax device could give rise to pressure for the adoption of tax supplements, thus requiring only one tax liability calculation with transmission of the proceeds of the different rates to the appropriate jurisdictions.

While the no-return withholding system, such as that used by St. Louis, reduces the number of persons who must file returns, there are still large numbers including all unincorporated businesses that must file multiple returns. Whether this is more annoying than filing for an entirely different kind of tax is subject to question, however.

Taxation of nonresidents.—One of the biggest selling points of the local income tax has been its ability to tax nonresidents who work in the city or taxing jurisdiction but live outside. There are arguments of equity involved in this provision, but the advantages of the additional revenue which would or does accrue to the taxing unit probably outweigh any questions of equity. This is particularly true when the revenue is derived under the very acceptable political rule of taxing "somebody else," particularly a nonconstituent.

While the equity arguments are not likely to rest heavily upon the taxing jurisdiction if it is able to tax nonresidents, they may and probably will be of importance to the State legislature in its determination of whether to authorize the local income tax and, if so, in what form.

The traditional arguments in favor of taxing nonresidents have been oriented around the central city-suburban relationships. It is emphasized that the city, the normal working place of suburbanites, must provide services—streets, transportation facilities, police, and fire protection—for its total daytime population. The wealthy residents have tended to move to the suburbs shifting with them the high residential property values and leaving the city with a reduced property base from which it must still supply all of the basic services. In addition, the population that remains or comes in to fill the vacuum, because of its lower economic status, presents additional problems of police and fire protection as well as increased costs for sanitation, health, and educational services. The only way to share these burdens equitably is to tax all of those who benefit from the cities' facilities, including the nonresident. The earnings tax becomes a very acceptable means for doing this.

In opposition to these arguments, it is pointed out that the greatest cost of government at the local level has to do with resident services—education, sanitation, and health. These burdens fall at the point of residence and the nonresident must pay for these services where he resides. It is unreasonable to expect that the nonresident should bear a double tax burden. As for police and fire protection, and sanitation service, the taxes on the commercial and business establishments more than pay for the services required by the nonresident. Further, the changing population pattern of the large city is not simply a problem to be borne by the surrounding suburbs. It is a problem which is statewide and nationwide in scope and should be borne by the total State and Nation. Much of the money spent for these additional services, particularly highways, health, and welfare does come from the State and Federal Governments. If additional help is needed, it should also come from these sources in order to spread equitably the burden.

It can be seen that some of these arguments which are in direct opposition could be, at least partially, answered on the basis of statistics dealing with the costs of services and the sources of revenue. The situation, however, varies from State to State and local unit to local unit so that specific statistics would have to be developed for each situation. General statistics may be misleading. The arguments are real and continuing and there will be strong pressure for taxing nonresidents because of the revenue windfall unless strong arguments (equitable and political) and statistics to the contrary force the State legislature, as in Pennsylvania,³⁸ to give priority to residence. In all cases under existing local income tax laws the nonresident is subject to the tax unless he is taxed at his place of residence, and even this exemption is not generally provided except in Pennsylvania.

Public acceptability.—The attitude of the public toward a tax may be as good a measure of its equity as any theoretical arguments. In the referendums that have been held, local income taxes have been approved as well as rejected. The decisions in these cases may involve more than equity, but the fairness of the tax should always be an important factor. In most cases the income tax will be compared with the property tax, since these proposals are usually made on the grounds of preventing an additional use of the property tax or in some cases even calling for a reduction. Lack of support for the local income tax does not necessarily mean support for the property tax, however. It may

³⁸ Except Philadelphia.

simply mean a reluctance to substitute the unknown for the known or be interpreted as a protest against governmental spending.

The local income tax has been rejected by referendum in several cities in Ohio; in Minneapolis and Duluth, Minnesota; and in Kansas City, Missouri. On the other hand, more cities have approved by referendum a local income tax than have disapproved, and once approved opposition to the tax seems to disappear. Only two citizens appeared to oppose the tax at public hearings in Toledo prior to reenactment for the years 1956-60 while in prior years the tax had been a campaign issue.³⁹ Voters in St. Louis supported the tax by a vote of six to one in 1954 after previous experience under a legislatively enacted tax, and increased this margin in 1959 to nine to one.

In the majority of jurisdictions where the local income tax has been used, the tax has been adopted by local legislative action without referendum.⁴⁰ A number of these adoptions have been made to recapture the tax for the resident community which would otherwise go to the community of employment, because in Pennsylvania the resident community takes priority in the event of double taxation. As nearly as can be determined by the literature available, the communities using the local income tax seem to accept it without undue criticism once it is adopted. This may be to some extent related to the fact that the rates of the tax are presently low, and it would remain to be seen what the reaction would be under conditions of substantially increased rates.

Incidence.—In the case of the individual, the local income tax should be borne largely by the initial taxpayer. While there may be some shifting through wage negotiations, many economists maintain that a personal tax, one that has no relationship to any business dealings, is not normally shifted.⁴¹ Net income taxes are considered personal taxes but in the case of earnings or wage taxes which are based on gross earnings, the incidence may be modified. Even with personal net income taxes there are complications which modify the basic rule of no shifting.⁴² Even the deduction of the local tax from State or Federal income taxes does not assure partial shifting because many persons take the flat rate deduction rather than itemizing. For all practical purposes it can be assumed, however, that the point of impact is the point of incidence for the local personal income tax.

³⁹ *National Municipal Review*, April 1956, p. 198.

⁴⁰ Pennsylvania's Act 481 authorizing these local taxes allows enactment by local ordinance procedure.

⁴¹ William J. Shultz and C. Lowell Harriss, *American Public Finance*, p. 154-155.

⁴² *Ibid.*, p. 172-173.

Since taxes on business relate to business transactions, there is always the possibility of shifting either forward in terms of increased product prices or backward through the reduction in payments for wages or raw materials. The profit margin (in the commonly used sense, not the economic) is going to determine the degree to which a particular business is going to absorb or attempt to pass on or back the tax increase. Its competitive position, whether local or national, will also determine its ability to modify prices or wages. Locally, a net income tax is likely to be self-equalizing among businesses, while nationally the competition with a nontaxed business could destroy a marginal operation. The incidence of the local net income tax on business will to a large extent be determined by the nature of the business and its efficiency of operation; but in any event, since it is always a net income tax for business, the effects should be minor in comparison with the Federal or State income taxes.

Economic Impact

Since the local income tax in all places except Pennsylvania falls on business earnings (net) as well as personal earnings, business concerns may have some direct interest in the application of the tax. In Pennsylvania, as well as the other States, businesses as employers will be affected by the costs of withholding and the possibility of higher wage costs if workers' net income is reduced.

Like other local taxes, it is difficult to determine the degree of influence which the existence of this tax will have upon business decisions. It is unlikely that the local income tax at its present very low rate is likely to affect the profits of a business severely enough to cause it to move, even where the business profits are directly taxed. The direct impact is not nearly as great as the local property tax in most instances, and the income tax has the further advantage that it is paid only when there is profit while the property tax comes due without regard to profit and loss.

Pressure for additional wages may be increased as a result of another deduction from the paycheck, but there is no evidence to support a proposition that this has been a significant factor up to the present time. The inflationary pressures of the postwar period have far overshadowed any local income tax pressures which might exist. Whether these taxes will become more significant in business decisions in a period of stability or deflation remains to be seen.

There is also the possibility that an earnings tax might influence the decisions of business executives because they would become subject to such a tax. The decision might be nonrational with respect to the actual business impact but important to the local community. It must be assumed, however, that this type of personal influence would be the exception rather than the rule and would only become important in decisions, for example in locations where, other factors being equal, the local income tax becomes the deciding point. The low, flat rate earnings tax is likely to have less personal influence on business executives than a progressive tax.

While a number of cities where the local earnings tax has been used have experienced a business movement away from the city, this movement is attributed more to other forces bringing about a suburbanization of business than to this or other taxes.¹¹ Permanent escape from a new tax becomes somewhat risky, if not impossible, since it is difficult to assure that the same tax or another even more objectionable may not crop up in the new location.

An earnings tax should be relatively nondiscriminatory within the local community utilizing the tax, though, to the degree it affects wage negotiations, a business whose costs are largely wages could be more adversely affected than one where wage costs make up a smaller portion of total costs. Any tax which affects business establishments may contribute to the competitive struggle between communities for new business if the adoptions of the tax are spotty, but there is once again no good evidence to show that taxes are likely to be the deciding factor in this competition.

Summary

The local income tax has proven itself to be the largest producer of revenue for a given percentage rate. This is because the tax, in practice, is applied at a flat rate to gross income of individuals and net income of businesses with almost no exemptions, resulting in a very substantial tax base.

The local income or earnings tax has been utilized by a wide range of taxing jurisdictions in six States, ranging from a city of over 2 million population down to school districts of fewer than 25 pupils.¹² The combination of a flat rate confined to

¹¹ John H. Poelker, Comptroller of the city of St. Louis, attributes the trend to "space and market factors, rather than tax factors." Statement dated October 23, 1959.

¹² School district information supplied by David E. Stafford, Director of Research, Pennsylvania Education Association.

earned income with the withholding device collecting 75 to 80 percent of the revenue in most instances has allowed the application of this tax to smaller jurisdictions than might at first seem feasible on a purely logical basis.

The major arguments of equity have hinged around the non-inclusion of certain income, primarily investment, and the lack of a progressive rate or basic exemptions. The earnings tax is not generally considered to be any less equitable than sales or property taxes even by its critics, and the potential increased costs or administrative complications have worked against adoption of these modifications. Only Washington, D.C., at the local level utilizes a progressive income tax, and most persons would compare this jurisdiction more with a State than a local unit for tax purposes.

Finally, the local income tax, while it does affect business directly or indirectly, would not seem to have undue influence on location or profit margin with its present low rates. This is particularly true when it is viewed as a substitute for an added property tax.

CHAPTER 7

Sales Taxation

THE GREATEST production of nonproperty tax revenue at the local level is through sales or consumer taxation. This source also provides the majority of all tax revenue at the State level. Sales or consumer taxation becomes extremely complex because of the wide variety of forms which it takes. It would be impractical and of little value to examine all of the types of sales taxes which exist; so in this study a division will be made between general sales taxes and selective sales taxes. In the latter category, which can be almost infinite in variety, only relatively few of the more important selective applications will be considered.

Defining the Taxes

The term "general" in the first category is relative but is commonly understood to apply to all sales except those specifically exempt. The exemptions may be quite broad so that the tax base of the general sales tax is relatively narrow, but the distinction between "general" and "selective" as used here will be that a selective sales tax will be placed on a specifically named item or items while the general sales tax will apply to all items not specifically exempted.

Some further clarification may be useful on the question of terminology. A general sales tax may exempt by various devices. It may, for example, by legal terminology apply only to tangible retail sales. This would automatically exclude wholesale transactions and personal services, such as drycleaning and television repair. Further exemptions, such as food items, may also be provided. A general sales tax law may specifically include certain items for purposes of clarification, but this would still remain a "general" rather than "selective" sales tax.

Gross Receipts

Gross receipts are frequently used as a basis for actually assessing a sales tax; so the question of where to place gross

receipts taxes as such is raised. Taxes on the gross receipts of businesses have long been used and do differ in some respects from sales taxes. Without getting into the details of incidence, it is normally expected, and often written into the law, that sales taxes will be paid by the consumer.¹ Gross receipts taxes, as such, are usually broader in coverage and imposed at low fractional rates. Gross receipts taxes might also be thought of as gross business income taxes and, as in Indiana, can even be extended as a gross personal income tax. In this study gross receipts taxes will be considered in the general area of sales taxes unless they are applied to personal income, in which case they will be categorized as income taxes. Admittedly, the line between income and expenditure taxes is thin, and the case of gross receipts taxes illustrates the problems of differentiation.²

Since almost all gross receipts taxes at the local level tax only business income, this study will consider local gross receipts taxes as falling under sales taxation. The possible application of such taxes to school districts will be briefly considered following the discussion of the general sales tax.³

Significance of Name

While the terminology is not critical so long as it is understood what is being taxed, for legal purposes the name of the tax may make a difference. The use of the terms "gross receipts" and "licenses" enable some jurisdictions to do what they could not do under the name of "income tax." These are technicalities of legal interpretation which are not examined here, but which may be important in some jurisdictions and are worthy of local consideration.

Use Taxes

A separate tax known as a "use tax" is generally enacted by States which have sales taxes, but not normally for local jurisdictions. This will be discussed in later sections, but it is primarily a device to prevent evasion by placing a tax on the consumer who

¹ There are frequently provisions which make it illegal for a retailer to advertise or indicate that he is absorbing the sales tax.

² Commerce Clearing House in its tax information compilations, for example, includes Indiana's gross receipts tax and Gadsden's (Alabama) local income tax under the general category "Sales, Use, Gross Receipts" and not under "Personal Income" or "Corporate Income." The basis for their categories is "gross" as distinct from "net" rather than "sales" v. "income." See *State Tax Guide*.

³ P. 90-94 below.

uses a taxable item within the taxing jurisdiction if he has not paid the tax at the time of purchase. This becomes a true consumption tax but is basically a supplementary device for enforcing the sales tax in most cases. In a few instances there is a tendency for a greater emphasis on the use tax as a device to get at formerly untaxable sales, but the sales tax, as such, remains the major tax collecting device similar to withholding in the income tax field. In either case the use tax will be considered as a part of sales taxation.

Excise Taxes

Finally, the term "excise" may also appear in sales tax discussion. This term is applied to a wide variety of Federal selective sales taxes, some imposed upon the manufacturer and some upon the consumer directly.⁴ Since most Federal excise taxes are levied upon the producer rather than the consumer directly or separately, there is some tendency to think of excises as applying to this type of tax. The term has had various meanings in its historical use, but in this study excises will be classified as a part of sales taxation, in particular, selective sales taxation. A number of selective sales taxes are collected at a level above the consumer, e.g., cigarette, alcoholic beverage, and gasoline; so point of collection will not be used as a basis of tax differentiation but rather as an aspect of tax collection.

Extent of Use

As indicated above, sales taxes are the most widely used non-property taxes at the State and local level. As of July 1, 1962, 36 States plus the District of Columbia were imposing sales taxes. These are all general sales taxes, except for Pennsylvania and Wisconsin which have adopted rather broad selective sales taxes with many specified items covered in a single law. The number of local units using the sales tax is continually growing and probably runs well over 2,000 at the present time if general and selective sales taxes are included.

A tabulation on general sales taxes made as of January 1, 1960, showed 1,750 local jurisdictions in 13 States plus the District of Columbia using such taxes. This included 1,620 cities, 128

⁴The so-called luxury taxes on furs, jewelry, cosmetics, and taxes on transportation of persons and telephone and telegraph, for example, involve separate payments by the consumer. The hidden or manufacturers' excises are also assumed to be paid by the consumer in most instances.

counties, and 2 school districts. One additional school district was involved in combination with a city in Alaska.⁵ There are perhaps no tabulations available which would give a fully accurate picture of the extent of sales taxation at the local level at any single point in time. Actually, no such precise measure or tabulation is necessary and the results would probably not be worth the time and effort necessary to compile. We know from available data that the use has been expanding and is now considerable.

In 1955, the Municipal Finance Officers Association estimated, approximately 900 municipalities of all sizes were using the sales tax.⁶ While this includes only municipalities, if the ratio of municipal to other local units in recent years existed then, it would increase the figure to about 1,000 jurisdictions. The 1960 estimate given in the previous paragraph indicated 1,750 jurisdictions and a January 1, 1961, estimate indicated about 1,920 jurisdictions.⁷ Even recognizing that these figures may not be fully comparable, the approximately 10 percent per annum growth rate which they indicate may be of some significance. A major portion of this growth has taken place in California and Illinois, but it is also evident elsewhere. Virtually all of this growth has occurred since 1945 when there were only two cities in the United States which were imposing a local sales tax.

It should be noted that the pattern of growth which has been presented thus far is that of the "general" sales taxes used locally. If the "selective" sales tax jurisdictions were added, the figure would be substantially increased, though there would be considerable duplication of jurisdiction, since a single jurisdiction may use both general and selective sales taxes. No compilation currently available throws all sales or consumption taxes together in the manner indicated in this study; so there is no comprehensive listing of jurisdictions utilizing either selective or general sales taxes.

In the discussion which follows the emphasis will be placed upon the general sales tax. After an analysis of this tax, the major selective sales taxes will be considered briefly, indicating the extent of their use and the variations and arguments which

⁵ Lennox L. Moak and Frank Cowan, Jr., *Administration of Local Sales and Use Taxes*, table 2, p. 10. The bulk of these jurisdictions are found in California and Illinois where 1,530 jurisdictions, cities, and counties, have taken advantage of those States' permissive legislation. The number of States and cities in Moak and Cowan's list should be reduced by one because Atlantic City, N. J. actually imposes a fairly broad selective sales tax rather than a true general sales tax.

⁶ Municipal Finance Officers Association, *Municipal Nonproperty Taxes*, p. 30.

⁷ Advisory Commission on Intergovernmental Relations, *Local Nonproperty Taxes*, table 17, p. 34.

might justify or deny the use of such taxes for educational support.

Present use of either general or selective sales taxes directly by school districts is, of course, extremely limited. At least four school districts in Alaska levy a general sales tax, but that is the only State where school districts directly levy such a tax. In several instances, particularly in New York⁸ (Monroe County and the city of Rochester) and Alabama, counties or cities may share a portion or all of their sales tax with the school district or districts involved. In Bristol, Virginia, the only city in that State to use the sales tax, schools benefit from the tax which is used exclusively for capital outlay. In several other States, selective sales taxes are used by local school districts. Pennsylvania districts utilize admissions and amusement, and real estate transfer taxes, and six city school districts in New York levy a consumer utility tax.⁹ Sharing of selective sales taxes in Alabama with schools also occurs.

None of this includes the dependent school systems which may theoretically share in such taxes but in practice generally do not. Sales taxes like income taxes make their main impact on local school districts through the indirect medium of State aid. It is quite common for State sales taxes or major portions of them to be earmarked for school purposes. There are many other cases where State sales taxes were sold to the electorate on the basis of supporting schools even though there was no legal earmarking.

General Sales Taxes

Some specific aspects of the general sales tax and its possible application to local school districts follow.

Potential Yield

The per capita yield of the general sales tax in cities over 10,000 population using this tax in 1955 was \$16.25, exactly the same per capita yield as the local income taxes for that same year. The local sales tax was used much more widely than the local income tax, however, and produced over 3.5 times as much total revenue. While the per capita yield equaled that of the income tax, this was achieved through a higher average rate which means

⁸ Arvid J. Burke, Mabel Walker, and Anne Phinney, "Local Nonproperty Taxes," p. 90.

⁹ Loc. cit. The Putnam County School Board in West Virginia levied and briefly collected a real estate transfer tax, but this tax has been declared unconstitutional.

that the local income tax was the greatest producer at the same rate. Interestingly, the rate differential was not great, 0.76 percent for the sales tax as opposed to 0.70 percent for the income tax. The range in rates of the sales tax for that year was from 0.5 percent to 3.0 percent, and the range in per capita yields was from \$1.83 to \$31.38.¹⁰

In 1957 general sales and gross receipts revenue for all local governments was estimated by the Bureau of the Census at about \$656 million. Of this, only \$494 thousand was attributed to school districts.¹¹ By 1960, three years later, this amount had risen to \$875 million for all local governments.¹² No census estimates for school districts are available for this type of detail except for years when a complete census of governments is taken. Per capita yields given by the Bureau of the Census for these years are not significant for estimating purposes because they are not confined to the using jurisdictions but rather represent aggregate figures. Some detail is available for 1960 in the form of yields for the large cities.¹³ Adjusted to an average rate of 1 percent the range of yield per capita for the 14 cities over 250,000 population that were using this tax in 1960 was from \$12.74 to \$22.91. Table 7 provides the detailed data.

Variations in the tax base will account for some of the difference in yield, and different economic patterns will account for the rest, but these are not things which can be put down with precision. The exemption of food, for example, will have a substantial impact upon the productivity of the general sales tax, while the marketing habits of residents and nonresidents will also affect the tax yield.

Exemptions.—The local sales tax, like the local income tax, is affected by exemptions and nonresident contributions. Unlike the income tax, however, solutions to the problems raised by these factors have generally reduced the yield of the local sales tax. Exemptions are accepted as a part of the local sales tax just as they are in a State sales tax, while the local income tax almost entirely ignores exemptions. The local gross receipts tax approaches a no-exemption policy, but when the rates get sufficiently high to compare it to the sales tax, there are usually variations in rates or methods of calculation introduced which

¹⁰ Municipal Finance Officers Association, *Municipal Nonproperty Taxes*, Appendix A, p. 24-25.

¹¹ U.S. Bureau of the Census, *U.S. Census of Governments: 1957*, Vol. III, No. 5, *Compendium of Government Finances*, table 46, p. 66.

¹² U.S. Bureau of the Census, *Governmental Finances in 1960*, G-GF60, No. 2 table 1, p. 16.

¹³ U.S. Bureau of the Census, *Compendium of City Government Finances in 1960*, City Finances: 1960 G-CF60—No. 2, Washington, D.C.: Government Printing Office, table 7.

Table 7.—Per capita yield of general sales and gross receipts taxes for selected cities: 1960

City	Actual rate	Yield (Thousands)	Population	Per capita yield at a 1-percent rate
New York.....	13.0	\$476,532	7,781,984	\$20.41
Chicago.....	0.5	22,627	3,550,404	12.74
Los Angeles.....	1.0	43,335	2,479,015	17.48
Washington, D.C.....	2.0	22,512	763,956	14.73
San Francisco.....	1.0	17,018	742,855	22.91
New Orleans.....	1.0	8,818	627,525	14.05
San Diego.....	1.0	8,452	573,224	14.74
Denver.....	1.0	5,434	493,887	11.00
Phoenix.....	0.5	3,928	439,170	17.88
Oakland.....	1.0	6,964	367,548	18.95
Long Beach.....	1.0	4,795	344,168	13.93

¹ Plus variable gross receipts tax.

² Includes yield of consumer utility tax.

³ Effective rate less than 0.5.

SOURCES: U.S. Bureau of the Census, Compendium of City Government Finances in 1960, tables 5 and 7; and Commerce Clearing House, State Tax Guide.

amount to the same thing as exemptions. The exemption question is removed from local control in a State collection system such as used in California and Illinois, since for uniformity purposes the State's exemptions become the local exemptions.

Certain exemptions such as direct sales to the Federal Government are dictated by constitutional interpretations¹⁴ while other exemptions, such as those to charitable, religious, and educational organizations, are dictated by the long practice and custom in other tax areas. A variety of other exemptions may be adopted because of effective political influence, arguments of equity and economic necessity, or both. Every exemption not only reduces the base of the tax and the yield but also opens a possible route for evasion and complicates administration of the tax. Certainly every requested exemption should be carefully examined as to its justification and ideally should be reviewed periodically to determine a continued necessity. An exemption once granted, however, is extremely difficult to remove.

Nonresident contributions.—The sales tax may under certain

¹⁴ In the pattern of exemptions for government-related activities, there are indications that the courts are moving from a doctrine of total mutual immunity to a doctrine of non-discriminatory taxation. See Karl E. Wolf, "Taxation of Contractors' Possession and Use of Government Property," p. 499-506; and *United States of America and Olin Mathieson Chemical Corporation v. Department of Revenue of the State of Illinois and Theodore J. Isaacs*, Director of Revenue, 202 F. Supp. 757 (March 7, 1962) as upheld by the U.S. Supreme Court in 371 U.S. 21.

circumstances produce revenue from nonresident sources, particularly if the local unit applying the tax is a market center for an area or a major tourist attraction. There is a counterforce at work, however, which is the pressure for residents to buy outside the local jurisdiction in order to avoid the tax. Virtually no evidence is available to indicate the real impact of nonresident spending. There is no question that cities which attract large numbers of tourists will benefit, particularly if the things which tourists buy are included under the tax, e.g., hotel and motel rooms, restaurant meals. In some cases these tourist items are separately taxed at higher than the ordinary sales tax rates through a selective sales tax. The daily commuter to the city may also contribute through the sales tax, but the amount is normally negligible, particularly in comparison with the impact of the wage tax upon a commuter.

Resident evasion.—For the normal pattern of everyday purchasing, the analysis is more complicated. There seems to be some evidence that the resident will travel in order to avoid the sales tax on his purchases but perhaps not too far.¹⁵ This will undoubtedly vary in relation to the size of the purchase and the rate of tax. If the differential in rate is sufficiently high, it is logical to assume that some trade will be transferred. In areas where purchases for delivery outside the taxing jurisdiction are untaxed, a frequent provision, there is a reported increase in deliveries by local merchants which involve not only increased requests from legitimate nonresidents, but also deliveries of commodities of residents to the homes of friends outside the taxing jurisdiction.¹⁶

No evidence has been published to show that this is a particularly serious problem from the point of view of tax yield. The factor of convenience would severely limit its use since this type of arrangement might involve a subsequent transfer of goods and an extra trip. In addition, the use of the very convenient charge account is sacrificed through this procedure.

Any interpretation of a movement of retail business to non-taxing suburbs must rest more upon a pattern of business than upon tax impact. The convenience of suburban locations and their particular adaptability to the heavy use of the automobile is the most ready and logical explanation of such developmental patterns, since they occur both in areas with and without local sales taxes. The implications of this pattern may be, however, that the

¹⁵ See p. 89 below.

¹⁶ Lennox L. Moak and Frank Cowan, Jr., *Administration of Local Sales and Use Taxes*, p. 15.

local sales tax jurisdiction must be large enough to encompass a major shopping center if it is to be productive.

Conclusions.—The actual yield of the local sales tax will depend upon what is included and excluded as well as the range of the tax, but it must encompass geographically the location of retail establishments where purchases are made. The use tax which would shift the locus of the tax to the residence of the purchaser is generally not available to local jurisdictions and is difficult to enforce except for very large items or purchases. As a consequence, any jurisdiction expecting to levy a local sales tax must have within its boundaries a substantial number of retail establishments if it expects to obtain the per capita yields indicated earlier. A general sales tax, since it does require substantial administrative enforcement, should probably not be utilized, at least on a locally administered basis, unless it would produce within the range of yields for the large city group. If State administered, almost any local jurisdiction could participate even though the per capita yields would in many cases be slight, since the administrative costs would be consolidated.

Administrative Feasibility

A local general sales tax is probably easier to administer than a local income tax, though any such conclusion would depend upon the features of the two taxes. A sales tax, like the income tax, is largely self-administered but has the added advantage of fewer respondents. Each retail business in the jurisdiction is required to file a return, normally monthly or quarterly, giving the amount of gross sales, deductible items, and tax collected. The number of such returns would in most instances be less or certainly no more than the number of returns involved in the withholding operation of the income tax. There would be no direct supplementary relationship with the actual taxpayer, the purchaser, as there is with the income tax unless a use tax is involved.

Use tax administration.—As noted, the use tax is actually a supplementary device designed to prevent the avoidance of the sales tax by residents who might choose to buy goods in nontax areas. The administrative experience under the use tax is in virtually all cases unsatisfactory, if success is to be measured by achieving a high percentage return on the total of outside purchases. In almost all jurisdictions the enforcement efforts are confined to catching large outside purchases, either in size or value. It may be assumed that persons will not travel any great

distance to avoid the tax unless the amount of purchase and therefore the tax is substantial. Shopping centers just outside jurisdictional lines may present some problem, but enforcement of the use tax against small purchases would undoubtedly cost more than the return in taxes. One of the largest items, automobiles, is relatively easy to control because of registration requirements and resultant available records of sales or transfer. The existence and possibility of application of a use tax may discourage any widespread movement to buy outside the taxing jurisdiction, and its value may lie in this direction rather than in the direct production of revenue.

Local administrative costs.—There has been enough experience with the local sales tax to develop some actual costs of administration, though even the published figures are frequently rough since it is often difficult to establish all of the actual administrative costs. General overhead items of government such as personnel services, rent and maintenance services, and enforcement activities (attorney general's services), as well as shared costs through interchange of personnel and multiple function units complicate the gathering of accurate cost figures. Table 8 lists some of the local jurisdictions for which administrative costs or estimates have been made.

Retailer collection discounts.—These costs of administration do not include discounts allowed to retailers for the cost of collection.

Table 8.—Local sales tax administrative cost as a percent of sales tax collected

Jurisdiction	Year	Revenue	Percent of revenue for administration
Atlantic City, New Jersey ¹	1958	\$1,566,689	5.05
Baton Rouge, Louisiana ²	1950	^a NA	1.30
Bristol, Virginia ⁴	1955	^a NA	2.00
California (local) ¹	1958	161,915,036	1.72
Denver, Colorado ¹	1958	4,826,048	2.68
Erie County, New York ¹	1958	10,441,434	2.18
Florence, Alabama ¹	1958	182,190	1.79
New Orleans, Louisiana ²	1950	^a NA	2.40
Newburgh, New York ²	1950	^a NA	3.10
Santa Barbara, California ¹	1958	969,896	.92
Tucson, Arizona ¹	1958	974,159	2.09

¹ Lennox L. Moak and Frank Cowan, Jr., *Administration of Local Sales and Use Taxes*, p. 87.

² Frederick D. Stocker, *Nonproperty Taxes as Sources of Local Revenue*, table 4, p. 42. (Newburgh no longer imposes this tax.)

^a Data not available.

⁴ Sam T. Bowman, *Sales Tax Administration in a Small City*, p. 112. Less than 2 percent.

Discounts may range as high as 5 percent and must be added to the total administrative costs where applicable. Arguments relative to the necessity of such discounts were examined under the section on administration of the local income tax and would apply to the sales tax as well.¹⁷

State collection costs.—A recent study on the State costs of collection of various taxes indicates a fairly wide range of reported collection costs for general sales, use, and gross receipts taxes for 1960. Including discounts or collection allowances, the range is from 0.77 to 6.53 percent. Excluding collection allowances, the preponderant majority of the States reporting (16 out of 24) indicated a range of collection cost running between 1.00 and 1.50 percent.¹⁸

When the experience reported by the local units is combined with the experience of the States, it would appear that a reasonable cost of administration would fall someplace around 2 percent, excluding discounts or vendor collection allowances. This percentage may rise considerably for very low rates or very small jurisdictions and may be reduced by enlarging the jurisdiction, unusually efficient administration, or minimal administration. The latter choice is to be avoided, of course, since it will also likely result in reduced tax reporting and greater inequity in application.

The problem of minimal administration at the State level is apparently a real one. The major enforcement instrument from an administrative viewpoint is the audit, and it has been shown that recoveries from audits far exceed the additional costs involved. Some examples of recovery ratios for 1959 are \$17 for each additional \$1 spent for audit in Alabama, \$7.50 in Mississippi, \$6.75 in Utah, and \$5.61 in North Carolina.

In spite of the recognized return in dollars, the States have been reluctant to provide adequate auditing staffs both in numbers and salaries. Half of the States do not reach what one authority considers a bare, inadequate minimum of 1,000 accounts per auditor. They range from one auditor for each 12,000 accounts down to one auditor for each 385 accounts. The percentage of accounts covered in the States each year ranges from 15 percent down to 0.4 percent.

Since most underpayment is not a result of deliberate fraud but rather the keeping of inadequate or inaccurate records, auditing becomes a very necessary enforcement technique. If

¹⁷ See p. 55 above.

¹⁸ National Tax Association, Third Interim Report of the Committee on Cost of Taxpayer Compliance and Administration, *Cost of Collecting Some of the Major State Taxes*, table 2. Collection allowances as indicated in footnote 1, table 1 of the report deducted.

large units such as States have been remiss in the application of this technique, there is a danger that the same pattern might be followed at the local level.¹⁹

A manual for local use.—The administrative problems of local sales and use taxes have been very thoroughly considered in a recent publication of the Municipal Finance Officers Association of the United States and Canada.²⁰ This manual presents in detail with sample forms a step-by-step procedure for establishing or improving a local general sales tax administrative program. While no manual could be expected to answer every question which might arise, the existence of such comprehensive and detailed advice as evidenced in this manual should ease the problems of any school district or other local government unit which might choose to utilize a general sales tax.

Conclusions.—If the potential sales tax yield for a school district is sufficiently large to make the sales tax an acceptable alternative or supplemental source of revenue, it would not appear that the administrative problems connected with the sales tax should inhibit its use, except in very unusual circumstances.²¹ One of the unusual circumstances might be where the addition of a local tax would make the prevailing total rate sufficiently high to force outside purchasing which would either result in reduced yield or increased enforcement costs through a use tax. Even these circumstances are difficult to accurately predict in advance of actual application.

Equity and Incidence

Equitability of the sales tax has been argued vigorously over the past several decades. Since the arguments are likely to be raised in any attempted adoption at the local level, it will be appropriate to review some of the more important points in this study.

Progressivity v. regressivity.—The sales tax has regularly and consistently been attacked on grounds of being regressive, meaning that the lower income groups pay a higher proportion of

¹⁹ Data on auditing taken from John F. Due, "Improving the Sales Tax," p. 52-55.

²⁰ Lennox L. Moak and Frank Cowan, Jr., *Manual of Suggested Practices for Administration of Local Sales and Use Taxes*.

²¹ John Due has indicated that he feels certain rules should be followed in the application of sales taxes by municipalities, and it can be assumed that they would be transferable to school district use, should such use become necessary. These rules are: (1) require State collection and administration, (2) set identical base with State tax and no exemption for outside delivery or use taxes permitted, (3) authorize counties to impose tax to reduce shifting of purchases for evasive purposes, and (4) require a uniform rate, if possible. See his "Improving the Sales Tax," p. 58.

their income in sales tax than the higher income groups. There have been a number of studies made in recent years relating the impact of the sales tax to various income groups. These have been done both on a theoretical basis and by utilizing a particular State's sales tax law.²²

The conclusion which can be drawn from these studies, although they differ in degree, is that a sales tax which includes food or food and utilities is regressive through the entire range of income groups. On the other hand, when food is exempt, the sales tax tends to become proportional for most of the income scale with some regressivity at the highest and lowest levels. One study shows an actual progression with food exempt and another some progression in the middle income ranges. Since it is the broad middle income group which bears the real tax burden in the United States, it is of some significance that the sales tax could be considered at least proportional for that group, if food is exempt.

While proportionality will not meet the equity demands of those who insist upon a progressive rate as the only measure of ability to pay, it does probably indicate that the regressive aspects of the sales tax have been overemphasized and are to some extent a carryover from the Great Depression period when many of the State sales taxes did impose the tax on food and when most incomes were low. Statistics may show a more moderate side, but the emotional pattern will still be significant in any adoption attempts. While exemptions, in general, add to administrative costs and pose complications, the exemption of food in a general sales tax is well worth considering by any jurisdiction anticipating adoption of the sales tax. Such an exemption may have a great impact on equity.

Shifting.—The question of who actually pays the general sales tax is closely related to equity. While the tax itself is paid by the dealer or retailer, it is expected that the retailer actually has collected the tax in the form of an additional and separate levy at the time of sale. Several States, in fact, prohibit a retailer, under penalty of law, from advertising or claiming to absorb the retail sales tax in the price of his product. These provisions are designed to keep the sales tax as a separately imposed con-

²² Various studies in this area have been brought together and summary tables prepared in several more general sources. See John Due, *Sales Taxation*, p. 25-29, tables I-V; Lennox L. Moak and Frank Cowan, Jr., *Administration of Local Sales and Use Taxes*, p. 13-14, tables 3-6; and R. A. Zubrow, R. L. Decker, and E. H. Plank, *Financing State and Local Government in Nevada*, p. 415-420, table 10.10. Two more recent articles which analyze this subject or aspects of it are Reed R. Hansen, "An Empirical Analysis of the Retail Sales Tax with Policy Recommendations," and James R. Beaton, "Family Tax Burdens by Income Levels."

sumer tax, and to theoretically maintain by legally enforced shifting the same competitive position among merchants that existed prior to the adoption of the tax. Where all merchants in a market area are covered by the same sales tax, it may in fact not affect the competitive position of any single one. Where jurisdictional lines cut through a market area, however, and one jurisdiction imposes a tax while another or others do not, then the merchant in the taxing jurisdiction may feel compelled to lower his prices somewhat for competitive reasons and thus in fact absorb some of the tax. No State law prohibits this if no claim of absorption is made.

In all States, whether required or not, the practice is to quote separately the sales tax to the consumer.²³ This may have advantages to the consumer as well as the retailer, since it also prevents price increases by adding the dealer's profit margin to the tax—a frequent occurrence in hidden excises. In practice the degree of shifting does not appear to be related to whether the tax is levied on gross sales or sales at retail. It can be assumed that in virtually all cases the sales tax is shifted to the consumer.²⁴

Effects on commuters.—The sales tax is sometimes justified on the grounds that it taps commuters and transient population who would not otherwise pay for the support of the many governmental services from which they benefit during their stay or which may be supplied to accommodate them. A sales tax which includes restaurant meals and tourist accommodations as well as a beginning rate for small amounts will undoubtedly collect some revenue from commuters and transients. Since there are no records relating residence in sales taxes paid, it is virtually impossible to estimate the amounts involved. It is doubtful whether these are substantial except in resort areas, but they may offset to some degree purchases by residents made outside the jurisdictions.²⁵

A balance for the progressive income tax.—As in the case of the flat rate income tax, it is usually noted that the regressive or proportional sales tax may simply add balance to the total tax system offsetting the very progressive Federal income tax. In rebuttal it has also been noted that while there is merit in considering the total effect of Federal, State, and local systems, in choosing the component parts which make up this system, the

²³ John F. Due, *Sales Taxation*, p. 302-303.

²⁴ This is the traditional theory of the incidence of consumption taxes. For a different view that maintains that the incidence falls on the factors of production, see Earl R. Rolph and George F. Break, *Public Finance*, p. 287-295; and George F. Break, "The Incidence of Consumption Taxes," p. 625-632.

²⁵ See additional arguments on taxation of nonresidents above, p. 65-66 and 77-78.

more equitable tax should always be preferred over the less equitable.²⁶

Attitudes indicated by referendum.—The verdict of the voting public through referendum is probably no clearer in the case of the sales tax than it is in the income tax. Sales tax adoptions have had their greatest rise when the decision can be made by local legislative assemblies. In Mississippi, for example, authority to levy the sales tax was first granted cities in 1950, but a three-fifths referendum requirement plus some other restrictions limited it to only a few cities. With a gradual removing of the restrictions, some 10 cities were using the tax by 1953. With the removal of the size of city requirement in 1954 and the referendum requirement in 1955, adoptions increased rapidly. Thirty-seven cities had imposed the tax by August 1956; 46, by May 1957; and 99, by January 1, 1961.²⁷

The situation in Illinois is even more to the point. Municipalities in that State were first given the power to adopt a sales tax by the legislature in 1947 but only through a required local referendum. Approximately a dozen cities attempted to adopt the tax, but all were turned down at the polls. In 1955 the legislature removed the referendum requirement and provided for a locally imposed, State-collected sales tax up to a rate of 0.5 percent if and as adopted by the municipality. Six months later, in January 1956, 617 cities were imposing the tax. By May 1, 1957, the number had increased to 919 and by January 1, 1961, to 1,120 plus 56 counties.²⁸ Over 90 percent of the municipalities in Illinois now utilize a local sales tax.

The above illustrations refer to local sales taxes for general municipal purposes. Would a sales tax devoted to education purposes fare better or worse at the polls? The recent experience in Alabama may throw some light on this question. Through State legislative action and constitutional amendments, counties and cities in Alabama have been able to adopt sales taxes for education as well as general government activities. A number of counties and several cities have chosen to earmark all or a portion of their sales tax for schools. In 1961-62 six counties held elections for sales taxes pledged to education. In three counties the tax was adopted and in three it was defeated. In nine other counties such a tax was adopted during the same

²⁶ R. A. Zubrow, R. L. Decker, and E. H. Plank, *Financing State and Local Government in Nevada*, p. 392.

²⁷ John F. Due, *Sales Taxation*, p. 324-325; and Advisory Commission on Intergovernmental Relations, *Local Nonproperty Taxes*, table 17, p. 34.

²⁸ John F. Due, *Sales Taxation*, p. 323-324; and Advisory Commission on Intergovernmental Relations, *Local Nonproperty Taxes*, p. 34-35.

period without elections. In addition, during this same period, local referendums were held in 17 counties and 8 cities on the adoption of additional property tax millage for education. Such millage was adopted in 12 of the 17 counties and 4 of the 8 cities.²⁹

One might draw the conclusion from the Alabama story that the sales tax is less popular than the property tax, but it would be unfair to generalize and extend this conclusion beyond Alabama where the property tax is relatively low. It would seem safe, however, to conclude from the experiences in Alabama and other States that it is easier to get a sales tax, and perhaps any tax, adopted by legislative action than it is by referendum. It is apparently a painful process for the voter to accept any new tax.

Abandonments.—The sales tax, once adopted, seems to have a good record of retention. There have been only 16 known abandonments of the local sales tax since the initial adoption of that tax by New York City in 1934. Several of these abandonments took place in the 1930's and six occurred before the tax had been in operation one year, including two cities where the tax was repealed before it was put into effect. Except for Bluefield, West Virginia, where the tax was ruled invalid by the courts, it has been indicated that the basic cause for abandonment was public and political pressure.³⁰ In Philadelphia there was organized opposition by retailers and labor unions.³¹ It is interesting to note that the two largest cities involved in abandoning the sales tax, Philadelphia and St. Louis, have both subsequently adopted the local income tax as a major nonproperty tax source.

Since most of the adoptions of local sales taxes have occurred since the abandonments noted above, whatever significance these abandonments might have is reduced even further. It would appear that the public antagonism which certainly existed in the first decade of the general sales tax has ameliorated to the point that the sales tax is not opposed *per se*, though, like any new tax, it is likely to be opposed by various groups within the community. Organized labor is still opposed to the sales tax as a matter of principle, while business, with the possible exception of retailers directly affected, tends to favor this tax form.

Summary.—As in the case of most taxes used at the local level, there are many aspects of equity which can be raised with respect to the sales tax. A broad based sales tax is in practice "regressive," but when food and medicines are exempt, it ap-

²⁹ "Report Card on Local Tax Elections," p. 12-13.

³⁰ Lennox L. Moak and Frank Cowan, Jr., *Administration of Local Sales and Use Taxes*, p. 11.

³¹ John F. Due, *Sales Taxation*, p. 327.

proaches proportionality at least for the wide middle income range and would not seem to be any more "regressive" than the other local taxes. Like the local flat rate income tax, it can be partially justified as balancing off the highly progressive Federal income tax.

The local sales tax does have the advantage of being highly visible since it is normally separately calculated and paid with each retail transaction. There is no deception as to how much tax is being paid as there is in the hidden devices of many excise taxes or even the withholding features of the income tax. Since the amounts paid are normally small, the pain inflicted upon the taxpayer is likely to be less sharp, however, than the property tax or the quarterly-declared income tax payments.

While the sales tax might not win a popularity contest among taxes, whatever such a contest might prove, the sharp hostility of the 1930's has certainly diminished to the point of wide acceptance and consideration.

Economic Impact

This section concerns what some writers have described as the indirect economic effects of the sales tax—the impact on the levels of expenditure or business activity, changes in consumption patterns, and possible discriminatory effects between different businesses.²² There are other economic effects which have been considered above under incidence and equity and administrative feasibility.

The broad economic effects such as those of an inflationary or deflationary nature are not normally of any great concern at the local level. These effects may be somewhat significant at the State level but are usually considered as of great importance only at the national level. Of course, the cumulative effects of widespread local adoptions might equal that of a national or Federal tax, but such an occurrence over a short span of time is unlikely.

Anti-inflationary nature.—Though agreement is not unanimous, there is an assumption that the sales tax is anti-inflationary under certain conditions—temporary, general wage increases avoided and general acceptability of the tax as an equitable inflation control device—and primarily because of its effect of discouraging consumption through higher prices and encouraging savings.²³ The possibility of meeting the necessary conditions reduces the

²² Governor's Tax Study Group, *Financing Government in Colorado*, p. 197.

²³ John F. Due, *Sales Taxation*, p. 42-48.

potential of the sales tax as anti-inflationary in practice, though, in general, it is considered less inflationary than the income tax.

Arguments are still being advanced that the sales tax could be a factor in the fast relatively noninflationary growth of the European economies and that the lessons might be applied in the United States in the form of a Federal sales tax.³⁴

That such factors are not given much significance at the State and local levels is illustrated by the fact that the general sales tax was introduced in the Great Depression of the thirties, without question more a matter of expediency than economic planning. It was certainly not a period, however, when deflation was desired. Even were the effects of the sales tax better documented, local jurisdictions would not need to concern themselves to any great extent with this aspect of economic impact.

Impact on local trade.—Of more concern to local communities is the effect upon business activity in the immediate area and possible discriminatory effects. If the tax is broad based, covering essentials and nonessentials, then it might be fairly assumed that any decline in purchasing activities would occur in the nonessential lines. Actually the same effect would occur with essentials exempted from the tax, if one assumes that the demand for a fixed amount of revenue would result in a higher rate applying to nonessentials only. In practice this type of consumption shifting is not likely to be noticed with the low rate of local tax ordinarily applied unless the area is economically depressed. In the case of selective sales taxes, not being considered at this point, the impact on particular dealers or businesses might be more evident and deeply felt.

To the degree that the sales tax affects business, this effect is borne almost entirely by the retail merchant. If certain types of services are covered, then they, too, will be affected. Industrial production concerns are unlikely to be affected except through some very indirect action such as a demand for higher wages because of increased taxes, unless one accepts a theory of incidence which differs from the traditional.³⁵ Retail merchants, on the other hand, could be affected if there are alternative markets available and *convenient* to the consumer.

Effect on shopping patterns.—Convenience is a very important factor in this equation. There seems to be some evidence that consumers will not shift or change their shopping pattern in order simply to avoid paying the local sales tax. Frederick D. Stocker reports the experience in Erie County with a 1 percent

³⁴ Henry C. Wallich, "For Fastest Growth—What Kind of a Tax?" p. 27, 139-40.

³⁵ See footnote 24, page 84 above.

tax and Syracuse with a 2 percent tax, and indicates that there was no appreciable change in volume of department store sales in the communities of the county where there was easy access to nearby taxfree communities. In Syracuse, which reduced its tax to 1 percent and ultimately repealed the tax, there was no indication that department store sales were influenced by the tax at any point.³⁶

On the other hand, the argument that a sales tax might adversely influence retail trade inside the city was used to help prevent New York City from raising its tax from 3 to 4 percent, and discourage the adoption of a sales tax in Baltimore, Maryland.³⁷ In Denver, Colorado, resistance by business firms has been negligible, perhaps because they can keep 5 percent of the tax collected as a collection cost reimbursement, but there was some increase in purchases made outside the city after the adoption of the sales tax in 1948. These purchases tapered off but not entirely, though business activity did increase each year in the city during that period.³⁸

A study made during the summer 1958 of the pattern of purchases by residents of border cities in the State of Washington tends to support the proposition that purchasers will change their buying habits if they can conveniently avoid a fairly substantial general sales tax.³⁹

There has been some concern occasionally expressed because of the increase in deliveries outside the taxing jurisdiction with the advent of the sales tax. Since some of these instances occurred shortly after World War II, there may have been some natural increase in demand for such services which were curtailed during the war. On the other hand, since the exemption of deliveries outside the taxing jurisdiction, which is included in many local sales tax ordinances, is given on behalf of the local merchant to avoid damaging his competitive position for outside sales, it is natural that the nonresident may choose delivery and no tax on some items which he might otherwise have carried. The delivery of small purchases is something which the retail merchant must regulate within his profit margins.⁴⁰

Delivery of purchases of residents to the homes of nonresident friends, a phenomenon sometimes noted in sales tax communities

³⁶ Frederick D. Stocker, *Nonproperty Taxes as Sources of Local Revenue*, p. 38-39. Syracuse has since reimposed the tax at 2 percent.

³⁷ Lennox L. Moak and Frank Cowan, Jr., *Administration of Local Sales and Use Taxes*, p. 15.

³⁸ Roy W. Cass, "The Denver Retail Sales Tax," p. 130-131.

³⁹ Harry E. McAllister, "The Border Tax Problem in Washington."

⁴⁰ The same may be said for the added costs or inconvenience of keeping separate records of exempt sales because of outside delivery.

with outside delivery exemptions, is a matter of tax evasion as well as extra dealer burden. For expensive nonbulky items the tax savings may overcome the inconvenience and outside deliveries may be used as an evasive technique. The existence of a use tax may have a persuasive effect on most citizens not to evade the tax even if the use tax is relatively unenforceable, but under any circumstance this particular type of activity will not adversely affect the merchant because delivery charges will be more than offset by the profit on expensive items. The problem becomes one of administrative enforcement, considered elsewhere.⁴¹

Summary.—The economic impact of the sales tax in this section has been considered primarily from the point of view of its noninflationary characteristics and its effect upon local business activities. It was noted that the broader economic factors evidenced by inflationary or noninflationary characteristics need not be seriously considered for local tax purposes, but that the sales tax is considered relatively noninflationary by some economists because it shifts emphasis from consumption to savings. While the tax revenue will be spent by the local government, the expenditures by the public sector may be quite different than the expenditures in the private sector.

Of more serious concern at the local level is the effect on local business. Only retail merchants are likely to be directly affected by a sales tax. The evidence relating to the shifting of buying patterns is mixed. There is still some fear of such movement if the rates of the tax are sufficiently high but limited experience to show what would actually happen.

The shifting patterns of retail trade from downtown to suburbs are more likely an outgrowth of changing residence and transportation patterns than anything else. The existence or non-existence of a local sales tax may accelerate or decelerate the trend, but it is not likely to stop or change it. Once again the level of the tax may be important but, since our experience has only been with relatively low level sales taxes, it is not known what the threshold of a rate rise might be. This evidence will have to await future increases and higher differential rates.

Gross Receipts Taxes

Gross receipts taxation as such usually refers to gross receipts business licenses. As a licensing activity, of course, such taxes

⁴¹ See page 78 above.

would be beyond the consideration of school districts. In fact, most such taxes whether in license or nonlicense form are designed for revenue purposes rather than regulation. Under these circumstances gross receipts taxes can legitimately be considered for school purposes if their advantages so warrant. Several school districts in Pennsylvania do use such taxes under the general title "mercantile tax."

Statistics on the use of gross receipts licenses are not too clear because there is some tendency to lump together all licensing revenue. This will include revenue based on a variety of measures other than gross receipts. Gross receipts licensing is utilized by municipalities in about 26 States,³³ however, and specific cases illustrate that yields can be substantial. Estimated per capita yields of business gross receipts taxes for municipalities ranked above all nonproperty taxes in 1955 except income and sales.³⁴

Relation to General Sales Taxes

The gross receipts taxes are in many cases closely related to sales taxes. In some forms it may only apply to merchandising operations, retail and wholesale, and in others it may cover the whole spectrum of business activity. Unlike the sales tax, however, it is applied to the business concerns directly. Since it involves a cost of doing business, the tax may be pyramided by the addition of markups to the increased cost base. This is particularly true where the tax is levied at both the wholesale and retail levels. While auditors may use gross receipts of a retailing concern as a measure of the amount of a general sales tax which should be paid, the tax itself is levied by the retailer on the consumer as a separate transaction and not included in the profit markup.

Yield of Tax

Normally, since the gross receipts tax covers a larger base, its rate is lower than the sales tax. In 1955 the rates ranged from .0014 to 3.0 percent with an average of 0.23 percent. This produced over \$145 million, averaging \$5.74 per capita for the 189 cities and equaled 11.58 percent of the property tax yield in those cities.³⁵ A general business tax of one-tenth of 1 percent

³³ Municipal Finance Officers Association, *Municipal Nonproperty Taxes*, p. 24.

³⁴ *Ibid.*, p. 33-35.

³⁵ *Ibid.*, p. 34.

produced \$6,812,612 in 1958-59 for the Philadelphia School District. The more restrictive tax of the Pittsburgh School District of one-twentieth of 1 percent on wholesalers and one-tenth of 1 percent on retailers produced \$1,689,607 in that same year.⁴⁵ All other school districts in Pennsylvania collected \$220,843 with rates running to a maximum of one-tenth of 1 percent wholesale, and fifteen-hundredths of 1 percent retail.⁴⁶ In 1958-59 the number of school districts levying such taxes in Pennsylvania was 19, excluding Philadelphia and Pittsburgh.⁴⁷

Since New York City has both a gross receipts tax and a sales tax, it is possible to compare the yields of the two taxes. New York's gross receipts tax makes certain deductions from gross (\$10,000 or \$5,000) and differentiates between financial businesses and all others on rates.⁴⁸ The general business tax which is based on a \$10,000 exclusion and a rate of two-fifths of 1 percent produces the bulk of revenue and this amounted to almost \$154 million in 1960. This can be compared with almost \$297 million produced by the 3 percent retail sales tax.⁴⁹ There seems to be little question that the gross receipts tax can produce substantial amounts of revenue.

That the base of a gross receipts tax is even so broad that it can outproduce, relatively speaking, a local income tax is illustrated by Philadelphia's position. Its income tax at a rate of 1.5 percent produced \$70.9 million in 1960 while its mercantile license tax at 0.3 percent was producing \$18.0 million.⁵⁰ A little simple arithmetic will show that the ratio between the rates and the yields indicate a larger percentage yield for the mercantile tax. This is also borne out by per capita figures, adjusted to a common rate, reported for these two taxes in 1955.⁵¹

Objections to the Tax

In spite of the very sizable yields of gross receipts taxes at even low rates, serious objections are frequently raised against

⁴⁵ Governor's Committee on Education, *Facts and Figures on Education in Pennsylvania*, Appendix 1 to the Final Report, p. 108. The Pittsburgh School District mercantile tax was repealed with the adoption of an income tax.

⁴⁶ *Ibid.*, p. 81; and David F. Stafford, "Financing Public Education in Pennsylvania," p. 2.

⁴⁷ David F. Stafford, "Financing Public Education in Pennsylvania," p. 2.

⁴⁸ Commerce Clearing House, *State Tax Guide*.

⁴⁹ Memorandum of Bureau of Educational Program Research and Statistics of New York City Board of Education dated May 24, 1961.

⁵⁰ U.S. Bureau of the Census, *Compendium of City Government Finances in 1960*, p. 60. Mercantile license tax figures for 1960 obtained from Office of the Director of Finance, Philadelphia.

⁵¹ Municipal Finance Officers Association, *Municipal Nonproperty Taxes*, p. 38.

these taxes. The major objection is that a flat rate gross receipts tax recognizes no differences between high gross, low profit margin and low gross, high profit margin business concerns. The former, it is claimed, are unduly discriminated against by the tax. Further and perhaps more serious, a business must pay this tax even if it earns no profit.

It is further argued that this like any business tax may place an excessive competitive burden on a local concern which is competing with outside concerns. Considering the nature of American business today, such competition is likely for all except local retailing, distribution, service, or recreation activities. Finally, as mentioned above, if the business firms are able to shift the burden of the tax to the consumer, the effects of pyramiding may make the tax on the consumer heavier than it would have to be if levied directly.

Rebuttal to Objections

In rebuttal it is sometimes maintained that the very low rates utilized limit any harmful effect on business. Payment of property taxes is also required whether or not a profit is made, and this is true of other fixed charges. The fixed nature of such charges gives a stability to the tax structure missing from taxes based on profits. This stability is important to local government. It may also reach some business activities which would not normally be reached by a property tax.

Like many business taxes it is possible to tax the nonresident consumer with a gross receipts tax, and to many this is desirable.

To meet some of the objections of the nonsensitivity of the gross receipts tax to varying levels of profits and volume, there have been various devices proposed and adopted to try to compensate for these variations. It has been noted in the examples above that there is a frequent distinction in rates between wholesale and retail activities. More refined techniques and elaborate classifications of businesses into alternate rates have been proposed including relating rates to average net income or average gross profits.²² Generally, however, these classification schemes become quite complex and cannot meet all the variations in individual businesses, though they may increase the equity in average application unless the classifications are politically inspired.

²² See James W. Martin, "Devising and Administering Municipal Gross Receipts Business Licenses."

Summary and Conclusions

Only one independent school district, Philadelphia, obtains substantial sums from a gross receipts tax.⁵³ This form of taxation has a major drawback to use by school districts in that it may be closely related to licensing, not a school function. Under any circumstances this tax will involve careful consideration of its impact on business, since it is primarily a business tax. If the rates are kept very low, then the business impact may not be significant but neither will the revenue.

Because of this the gross receipts tax is perhaps best left to general government as a large revenue producer. In this way the ramifications of the tax will not influence any particular function and the political forces which are almost certain to be engendered by any large-scale business taxation can be funneled through normal governmental channels rather than the school administration.

⁵³ While authorized for use by school districts in Pennsylvania under Act 481, the mercantile (gross receipts) tax is one of the least widely adopted taxes among those available.

CHAPTER 8

Selective Sales Taxes

HAVING EXAMINED some aspects of general sales taxation, one can then compare and relate this tax to the selective or special sales taxes which are prevalent throughout the country. The variety of such taxes is almost without limit, theoretically. Any item which is consumed could be singled out for special taxation and a wide variety of such items have been so taxed, historically. There are practical limits to such taxation, of course, and these limits are tied to administrative feasibility. In general terms only items which are manufactured or which pass normally through relatively limited business channels are susceptible to efficient selective sales taxation. A tax on tomatoes, for example, might encourage a boom in home gardening and make tax enforcement extremely expensive. A tax on oranges or other citrus fruits, while perhaps objectionable on other grounds, would be administratively feasible because the marketing is channeled through a relatively few sources and widespread private cultivation is limited.

Some taxation which may have regulatory as well as revenue purposes may go beyond the point where it is efficient from a revenue point of view to administer, but the regulatory aspects become a justification for unusually high enforcement costs. Alcoholic beverage taxes in the United States undoubtedly reduce total legal consumption of such beverages, thus a regulatory aspect is involved. Such beverages, however, can be produced quite cheaply in a variety of ways by private individuals, and because of the high tax differential involved extensive evasion exists and enforcement costs mount.

No tax is able to reduce consumption entirely without exorbitant enforcement costs unless there are severely limited sources of the product. In cases where regulation is desired to the point of abstinence, therefore, direct legal prohibition and the necessary enforcement apparatus are used. A tax on opium or marijuana would not be considered by most persons as either a desirable form of regulation or of revenue. This study is not

directly concerned with the regulatory aspects of taxation, but it must be kept in mind that in the case of selective sales taxation there may be a reduction in the consumption of the particular item taxed and this may have implications beyond the reduction of potential revenue. In the case of general sales taxation, there may be some reduction in total private consumption and a shifting in consumption patterns because of differing individual priorities; but these patterns are rarely predictable and the tax is therefore nondiscriminatory, if it is truly general. These non-revenue aspects may be sufficient reason in many instances for school districts to shy away from selective sales taxes and leave them to general government support.

Arguments of Equity

From the point of view of equity the selective sales taxes may differ from the general sales tax. One argument for selective sales taxes is that they can be levied on luxury or nonessential items and some choice is then given to the individual in purchasing these items. If the tax is regressive, it is by choice. It must be recognized, nevertheless, that selective sales taxes are almost always levied on items where there is a high demand, for example, gasoline, cigarettes and tobacco, alcoholic beverages. That there is a high demand for these items would indicate that there may be some difference of opinion as to what can be considered necessities. If there were not a high demand, there would be little basis for levying the tax, at least from the point of view of revenue production.

Regressivity

Some selective sales taxes may be considered even more regressive than the general sales tax since the tax is imposed as a flat rate per unit without regard to price, for example, dollars per proof gallon of alcohol, cents per thousand of cigarettes. The lower income individual who purchases a cheaper brand will still pay the same tax as the person who buys a more expensive brand. Wide variation in actual buying habits makes assessment of regressivity somewhat difficult in the case of selective sales taxes. Actually, they probably follow a pattern similar to the general sales tax on the average but because of the wide element of choice involved may have a wider range of regressivity on the basis of income groups or of separate family incomes. In some

cases the tax can be avoided altogether, e.g., alcoholic beverages, tobacco or admissions, a rare, if not impossible, occurrence for the general sales tax. At the other extreme a very high proportion of income may be devoted to such taxes.

Visibility

There is another distinction between selective and general sales taxes which should be mentioned. As noted in the discussion on general sales taxes, the practice is to quote separately and collect the tax at the retail level, even though gross receipts may become or be the practice for determining the retail merchants' liability for the tax to the governmental unit concerned. As a consequence, the general sales tax is highly visible to the taxpayer. In the case of the selective sales tax, the tax is almost always included in the retail price of the goods and is normally collected at the manufacturing or wholesale level.

In spite of efforts to indicate the amount of tax being paid by signs on the gasoline pumps, printing on admission tickets, or stamps on packages of cigarettes¹ (local or State), the selective sales tax is much less apparent and visible to the taxpayer than the general sales tax. The major exception to this rule is the Federal "luxury" taxes which are separately stated and separately collected at the retail level.² With a few other exceptions,³ Federal, State, and local selective sales taxes tend to be hidden. These vary from manufacturers' excise taxes, which most persons do not know even exist, to separately stated taxes blended into a retail sales price which is frequently rounded to accommodate but also further deemphasize the tax.

The fact that selective sales taxes tend to be less visible than general sales taxes has both advantages and disadvantages. Invisibility created by applying the tax at the manufacturers' or wholesale level frequently results in a retail price higher than just the tax because profit calculations at the various levels from manufacturer down to retail utilize the tax as well as the basic price of the item for markup purposes. This is known as tax pyramiding. On the other hand, it may be possible to extract additional amounts of revenue from the public if they are unaware of the amount of tax being paid. Administration of the hidden tax is also normally simplified because it is collected at a

¹ Abolished at the Federal level but still used in some States and localities.

² The Federal transportation taxes also tend to be separately stated but not to the same degree as the "luxury" taxes.

³ For example, hotel room taxes and deed transfer taxes.

level where there are very few taxpayers and records are better kept. Many persons emphasize, however, that in a democracy the public should be aware of the taxes they pay, and this knowledge becomes one instrument useful in keeping government efficient. Whether limitation of funds, *per se*, results in more efficient activities, however, is still moot.

Some of the types of selective sales taxes which have been used are examined below. The list of such taxes is not comprehensive, but the more important of those in fairly common use are considered and related to possible application by school districts.

Motor Vehicle and Gasoline Taxes

Included in this category are three separate taxes or licenses instead of one—motor fuel taxes, motor vehicle licenses, and motor vehicle operators' licenses. No school district, so far as the author has been able to determine, levies any of these taxes directly at the present time though they do receive revenue from a local gasoline tax imposed by a few Alabama cities. Operators' licenses are levied only by States and the District of Columbia, but local (county and municipal) motor fuel taxes and motor vehicle licenses do exist in a number of States. This category of revenue produces substantial sums nationally. Table 9 gives the breakdown for these items by Federal, State, and local levels.

While the amount of money raised from these sources is substantial and considerable potential may still remain, the availability of revenue for educational purposes would seem to be limited. In some States a portion of such revenue, for example, the fees for learners' permits or fees added to drivers' licenses or automobile registrations, may be earmarked for driver educa-

Table 9.—Motor vehicle and gasoline taxes: 1960
(Millions of dollars)

Tax	All government	Federal government	State government	Local government
Total.....	7,052	1,984	4,908	160
Motor fuel.....	\$5,352	\$1,984	\$3,335	\$33
Motor vehicle licenses.....	1,595	-----	1,468	127
Operators' licenses.....	105	-----	105	-----

SOURCES: U.S. Bureau of the Census, *Governmental Finances in 1960*, table 1; and *Compendium of State Government Finances in 1960*, tables 6 and 7.

tion courses which are, of course, directly related. In general terms, however, the pattern has developed of earmarking these sources for construction of highways and related activities. The Federal Interstate Highway Program is being financed by a special trust fund created by a special Federal tax on gasoline.

Earmarked Funds

The problem of earmarked funds is one which can be argued at length, and there are patterns of earmarking in educational finance which would make the arguments appropriate here. Without getting into the arguments, however, one can note that neither in the case of highways nor in the case of education are the earmarked funds sufficient to pay the costs of the programs involved. The effect of earmarking may be more nearly one of limitations on expenditures rather than the reservation of sums of money which might be better used on some other program. While some imbalance in programs can and does occur in the States, the definition of imbalance is to a high degree political, and there is no indication that a major cause of the imbalance is earmarking. Certainly the demand for both highway and educational expenditures is higher than the present appropriations.

While the earmarking of taxes has theoretical and practical objections, a case can be made that the gasoline tax is more nearly a service charge or toll than a tax because of the close and direct relationship of the taxpayer to the facilities financed. It has also been pointed out that the gasoline tax is a very nominal toll and that, if toll roads were supported by taxes from the gasoline consumed on them rather than tolls, it would require more than 20 cents additional per gallon.⁴ There is no question of the direct relationship between motor vehicle and operators' licenses and highway construction and maintenance.

Conclusions

Without justifying the earmarking of taxes in general terms, it would seem reasonable and practical that little could be gained in trying to tap highway revenue for educational purposes beyond the highly specialized exception, driver training, which has been mentioned. As a consequence, no useful purpose would be served in analyzing these particular sources of revenue in detail. As table 9 above indicates, little use of these sources is made at the

⁴ See E. M. Cope, "The Gasoline Tax in Perspective."

local level. If there is to be a change in the pattern of highway user taxes, it would probably be more appropriate to expect a conversion in the direction of supporting the State general fund rather than earmarking for another function or being made a local source of revenue.

Cigarette and Tobacco Taxes

Tobacco taxes produced some \$65 million in revenue for local government in 1960.⁵ While school districts did not levy these taxes, they shared in them directly in a few instances in Alabama where some county and city cigarette taxes were earmarked for schools and indirectly in theory through a dependent relationship in Maryland. The Federal Government raised almost \$2 billion and the States almost \$1 billion from these sources.⁶ At the State level these taxes have occasionally been earmarked for schools.

While some potential for additional taxation and revenue still exists, it should be noted that in the case of cigarettes, particularly, a major portion of the wholesale cost is now made up of tax.⁷ In spite of cancer and other medical controversy, tobacco products provide a fairly stable source of revenue. These taxes were imposed by municipalities and a few counties in 11 States in 1955.⁸ The number of States with independent local cigarette or tobacco taxes has apparently been reduced to eight at the present time.⁹ Maryland and Minnesota do distribute part of the proceeds of the cigarette tax back to the cities and counties.

Administration of Tax

The local administration of cigarette and tobacco taxes is relatively simple from a mechanical point of view. In most instances the wholesale distributor is made responsible for applying or imprinting a tax stamp indicating payment. If cigarettes are acquired outside of the tax jurisdiction for resale, it may be necessary for the retail dealer to buy and apply the stamps. This

⁵ U.S. Bureau of the Census, *Governmental Finances in 1960*, table 1.

⁶ Loc. cit.

⁷ One author in a recent article maintains that tobacco taxes bear a relatively smaller burden today in this country than formerly. He advocates increasing tobacco taxes to give some relief to the income tax, and notes that foreign countries tax tobacco products at a much higher rate than we do. Martin Norr, "Tobacco Taxes at Home and Abroad."

⁸ Municipal Finance Officers Association, *Municipal Nonproperty Taxes*, p. 21.

⁹ Commerce Clearing House, *State Tax Guide and State Tax Review*.

would most likely occur in smaller tax jurisdictions. Some counterfeiting of tax stamps has been reported, but this does not appear to be a major problem.¹⁰

Discounts.—A discount, as high as 10 percent, is usually allowed the dealer or wholesaler on the stamps purchased to compensate for the expenditure involved in application and record keeping. In Florida the State administers the collection of the tax for the cities and counties using it, and deducts 2.5 percent as a collection cost.¹¹

While considerable savings could probably be made at the State level by adopting the Federal procedure of not applying tax stamps, this may not be feasible at the local level. The ease of transporting cigarettes to retailers may necessitate some identification that the local tax has been paid unless all wholesale distributors are located within the local jurisdiction.

Evasion.—One of the greatest problems in connection with the local tobacco taxes is the ease of evasion and the difficulty and expense of enforcement in the event of evasion.¹² As in the case of the sales tax, it is the tax differential which is significant. Since the percentage rate of these taxes, particularly the cigarette tax, is relatively high, there is more incentive for evasion than with the sales tax. A 3 cent tax on a package of cigarettes will ordinarily mean a tax of between 12 and 15 percent at current prices. Since the packages are relatively small, detection of evasion becomes difficult and expensive.

On the other hand, since cigarettes are an item of regular consumption by most smokers, purchases will frequently be made near the point of consumption as a matter of convenience, especially where machines are available. It is the regular commuter who is most likely to take advantage of any price differential between his residence and place of work because even with the high rate of tax, a trip is not warranted in dollars and cents unless quantity purchases are made. These quantity purchases become somewhat more difficult to conceal and can bring at least token enforcement.

¹⁰ Municipal Finance Officers Association, *Municipal Nonproperty Taxes*, p. 21.

¹¹ The 10 percent figure is reported in Municipal Finance Officers Association, *Local Nonproperty Taxes*, p. 21. In 1959 the average discount given by States for cigarette stamps was 4.6 percent with a median of 5.0 percent and a range of from 2.3 to 10.0 percent. The three States which did not use stamps or imprinting still allowed a discount, though of only 1 or 2 percent. See R. A. Zubrow, R. L. Decker, and E. H. Plank, *Financing State and Local Government in Nevada, 1960*, table 11.16, p. 464.

¹² See Warren A. Law, "Evasion of the State Tobacco Taxes," for an account of the enforcement difficulties which the States have met with respect to State tobacco taxes. Many of the important battles have been won, but the administrative problems remaining are still significant.

Emphasis on Cigarettes

In discussing tobacco taxes one is in practice discussing the cigarette tax. Forty-seven States out of the 50 have taxes on cigarettes, but only 16 States tax tobacco products other than cigarettes.¹³ There seems to be relatively little interest in the taxation of tobacco products other than cigarettes. This may be because of the "sin" onus historically attached primarily to cigarettes and not other tobacco products, but this aspect would be of lesser significance today. It can also be pointed out that a high tax on snuff and chewing tobacco would be highly regressive because of the income groups using these products. The tax on cigars which now approaches an ad valorem levy is probably less regressive than the cigarette tax. The social costs resulting from fire losses by careless smokers, an established fact, and the claims of medical damage or aggravation are sometimes used as justification for the high cigarette tax. Other tobacco products have little relationship to these factors.¹⁴

The major reason for emphasis on the taxation of cigarettes is probably related to consumption. Out of the 11.58 pounds of tobacco consumer per capita in 1960, 9.61 pounds or 90.8 percent was in the form of cigarettes. This can be compared with 21.8 percent in 1920 and 2.2 percent in 1900.¹⁵ It would seem that neither "sin" nor taxes has had any appreciable effect on the patterns of tobacco consumption in this country.

Application to Schools

When one considers the consumption pattern indicated above and its relation to yield, it is highly unlikely that many local jurisdictions would consider any tobacco tax except the cigarette tax and this has been basically the pattern up to the present time. The per capita yield of this tax in 1955 for municipalities above 10,000 averaged \$1.89 at an average rate of 2.6 cents per package. The yield per penny of tax tended to decline in the smaller communities, particularly below 25,000 population, but in the larger communities averaged over \$1.¹⁶ Its usefulness to the small school district, even if acceptable on other grounds, would have to be judged as extremely limited.

¹³ Commerce Clearing House, *State Tax Guide*.

¹⁴ For a more comprehensive treatment of the questions of equity involved in tobacco taxation, see Warren A. Law, "Tobacco Taxation in the Revenue System."

¹⁵ U.S. Bureau of the Census, *Statistical Abstract of the United States*, 1961, table 1108, p. 802.

¹⁶ Municipal Finance Officers Association, *Municipal Nonproperty Taxes*, Appendix A, p. 34.

Alcoholic Beverage Taxes

Of great importance in the total production of public revenue, taxes and license fees directly related to alcoholic beverages produced almost \$3.8 billion in 1960. This area of revenue is predominated, however, by the Federal Government with State governments taking \$650 million and local governments only \$23 million.¹⁷ No school district directly levies a tax on alcoholic beverages, but several districts in Alabama receive all or portions of such taxes levied by the counties or municipalities but earmarked for schools. There is also some *theoretical* sharing of these taxes under dependent relationships.

Sociological Factors and Enforcement

Taxation of alcoholic beverages has a long history in this country, beginning with the Federal tax on whiskey which resulted in the Whiskey Rebellion of 1794. Repealed in 1802 and reimposed for a period during and after the War of 1812, the Federal whiskey tax was once again imposed during the Civil War and has remained in effect since that period, though with changing rates.

The whole process of taxation of these items has become enmeshed in the sociological and emotional problems related to the consumption of alcohol, not to mention the religious feelings involved. As in the case of tobacco products, there is probably no significant opposition to the taxation of alcoholic beverages but there is considerable concern with the level of taxation. The rates of taxes on alcoholic beverages vary, with beer and light wines at a relatively low rate and distilled liquors at the high end of the scale. Taxes on distilled liquors were estimated at "500 percent of the cost of preparing liquor for the market" in 1953.¹⁸ While the relationship to the retail price is considerably less, even today the taxes on whiskey will average over 50 percent of the retail price. Federal excises have been reduced slightly since 1953, but State and local taxes have increased somewhat.

Tax rates on alcoholic beverages present an interesting study relative to the limits of selective sales taxation on items of strong demand.¹⁹ Neither prohibition nor high taxes have been able

¹⁷ U.S. Bureau of the Census, *Governmental Finances in 1960*, table 1, p. 16.

¹⁸ Walter F. Terry, "Liquor Taxes—Discriminatory, Inequitable, Excessive, and Self-Defeating," p. 14.

¹⁹ Per capita consumption has remained fairly steady over the past decade with some slight increase in distilled spirits and wines and a slight decline in malt liquors. U.S. Bureau of the Census, *Statistical Abstract of the United States*, 1961, table 1105, p. 801.

to stop the consumption of alcoholic beverages in the United States, though they both may have had an effect on *legal* consumption. There is no question that prohibition affected legal consumption, but there is less clarity in the case of the effect of taxation on illegal production and consumption. There is an assumption on the part of many persons that high taxes on these products do result in excessive evasion and revenue loss as well as encouragement of crime.²⁰

It is not the purpose here to analyze the broader aspects of liquor taxation and there are some conflicting claims. Seizure of illegal stills, both in number and gallons of mash, by Federal agents—there are no comprehensive State figures—has shown a decreasing pattern in recent years.²¹ There has been a geographic pattern involved in these seizures which may indicate a factor of taste as well as a tax evasion.²² Seizures which increased in the postwar period up until 1957 never reached prewar patterns when taxes were much lower,²³ but economic patterns and a carryover from the prohibition period may account for this. The strict control of raw materials during World War II virtually eliminated moonshining for a period of time.

Border Enforcement Problems

In addition to the evasion of taxes through illegal manufacture, there is some evidence that differential State rates, though much lower than the Federal, affect buying patterns in border areas.²⁴ Several States make a token effort at enforcement, some with special units for the purpose, but mainly concentrate on large-scale evasions. Legal allowances for out-of-State purchases, if fully exercised, could mean considerable loss. Enforcement of alcoholic beverage taxes by local units would be even more difficult.

Potentialities for Local Use

When the overall picture with respect to alcoholic beverage taxes is examined, the potentialities for local use becomes rather

²⁰ See Walter F. Terry, "Liquor Taxes—Discriminatory, Inequitable, Excessive, and Self-Defeating," p. 14; and William H. Kennedy, "An Introduction to the Problem: A Resume of the Federal Liquor Laws and Their Application to the Industry."

²¹ The decrease in seizures and arrests is attributed to a change in enforcement pattern begun in 1957 concentrating on large-scale operations, criminal prosecutions, and prevention of acquisition of necessary raw materials for illicit activities. U.S. Treasury Department, *Annual Report of the Secretary of the Treasury, June 30, 1961*, p. 198.

²² See Joseph P. McKenna and Francis M. Boddy, "How Bad Are Liquor Taxes?"

²³ *Ibid.*, table 3, p. 35.

²⁴ An estimate was made in 1953 that one store across the line from Minnesota was probably costing the State \$21,000 a year in reduced taxes. Dudley C. Ericson, "The Federal Whiskey Tax Rebellion from the Viewpoint of the States," p. 27.

limited. As a matter of fact the major local revenue possibilities are confined largely to licenses and taxes on beer and light wine.

Patterns of control.—The pattern of alcoholic beverage production and distribution is highly controlled at the Federal and State levels, perhaps more closely controlled than any other industry. These controls stem not only from the tax situation but also from legal limitations on use. Government derives revenue from the alcoholic beverage industry basically in three ways: (1) Taxes on production or sales, (2) licenses, or (3) profits from monopoly stores.

The Federal Government derives virtually all of its revenue from this source through excise taxes, though there are nominal license fees imposed on manufacturers, wholesalers, and retailers connected with the industry.

After the repeal of prohibition the States divided into two groups: (1) Those that licensed the industry and received their major revenue from special taxes on the product and (2) those that took over the wholesale or retail sale of alcoholic beverages, particularly the distilled liquors, and took their revenue in the form of profit on the sales involved.²⁵ The latter group normally allows the private sale of malt beverages (beer) and light wines, and there are some instances of local alcoholic beverage control (monopoly stores) under the license system States.

Local application.—If distilled liquors were considered as a local revenue source, as a practical matter taxes could only be imposed in the 32 States using the license system.²⁶ Further, they would have to contend with the relatively high Federal and State taxes already imposed. These factors, combined with the fact that some municipalities have used liquor licenses as a source of revenue and others share in the States' liquor taxes, have kept the number of local units using taxes on distilled spirits extremely low. Only 37 municipalities over 10,000 population in 1955 used an alcoholic beverage tax of any kind. These were almost all on beer and concentrated in three States—Alabama, Georgia, and Tennessee.²⁷

Conclusions.—When one considers the level of taxes already imposed and the problems of evasion and enforcement, and ignores the policy question of whether the support of education

²⁵ There was originally a third group, the prohibition States, but only one State falls in that category today, Mississippi, and that State derives considerable revenue from a special tax on illegal sales, so may in practice fall in the first group. Light beer is legal in Mississippi.

²⁶ Only seven States were using any type of direct local alcoholic beverage tax not counting California, where the local sales tax could be made applicable to liquor sales. Municipal Finance Officers Association, *Municipal Nonproperty Taxes*, 1955, p. 27.

should be closely tied to a highly controversial tax source with all the complexities of equity involved, he can, except in unusual cases, largely dismiss taxes on alcoholic beverages as a potential revenue source for local school districts. Where such taxes might be considered, the problems of equity and particularly regressivity will be much the same as with tobacco products, though the emotional factors are likely to be even more extreme.

Admissions and Amusement Taxes

There seems to be widespread agreement that taxes on admissions and amusements are particularly well adapted to the local level. It is usually pointed out that the events or activities taxed occur at the local level, affect primarily the local level, and are best enforced at the local level. The sometimes elusive and itinerate nature of many of these activities, such as traveling shows or special productions, require an alertness to local events which often cannot be achieved at the State or Federal level. From the point of view of administrative feasibility, there seems to be little question but that the local unit is as well if not better equipped than State and Federal units to administer these taxes.²⁷

While these taxes are widely used by municipalities²⁸ and to a limited extent by school districts²⁹ and other local units, the Federal Government has for many years collected the largest share of such taxes. At the peak of Federal collections on these sources, the revenue from the admissions tax alone produced almost \$400 million. This had slipped to less than one-tenth that amount in 1960.³⁰

The decline in Federal collections has resulted from two major factors. As a result of some pressure to move out of tax areas useful to the States and to adjust wartime rates, the tax on amusements has been reduced to 10 percent on amounts over \$1 from the former rate of a flat 20 percent. Also of importance was the decline until recently in movie patronage which had comprised the bulk of admissions in the earlier periods. This latter factor has had an impact on State and local revenues and

²⁷ See Frederick D. Stocker, *Nonproperty Taxes as Sources of Local Revenue*, p. 47-48, for opinions as to the superiority of local control.

²⁸ The last available count showed 688 municipalities in 17 different States using the admissions tax in 1956, Municipal Finance Officers Association, *Municipal Nonproperty Taxes, 1956*, p. 19.

²⁹ In Pennsylvania 168 school districts levied an amusement tax and 18 districts a tax on mechanical devices in 1957-58. David F. Stafford, *Financing Public Education in Pennsylvania*, p. 2.

³⁰ U.S. Treasury Department, *Annual Report, 1960*, table 15, p. 467.

has possibly discouraged some further entry into this field by local units in the wake of Federal withdrawal. There has been a recent upturn in motion picture attendance which may mean a renewed interest in this source in the future.

Limited Yield

The major drawback to the admissions and amusement taxes has been their relatively low yield. The per capita yield at an average rate of 5.86 percent in 1955 was only \$0.86 for all cities over 10,000 population. The range in per capita yields for these municipalities was from \$0.02 to \$6.91 at rates ranging from 2 percent to 20 percent.¹¹ These taxes only produced approximately \$41 million for State and local governments in 1957, the last year for which such detail is available.¹² Of this, approximately \$26 million was collected by local governments.

One of the factors which reduce the net yield of admissions and amusement taxes is the frequently limited base. In many places the main element of the base has been motion picture theaters. As these theaters closed or changed to drive-in operation in the postwar period, the base for the particular local government concerned was frequently decimated. To some extent the base was lost to all by reduced attendance, but in the case of the shift to drive-in theaters, one jurisdiction's loss became another jurisdiction's potential gain.

Even more important, however, has been the change in amusement tastes which have occurred in the postwar period. The tremendous growth of participation in bowling and golf can be cited as examples. These activities have rarely been taxed as amusements, though they certainly could qualify in any broad definition of the term, and in the case of golf and some forms of bowling have even been publicly subsidized.

Pinball machines and gambling devices or games have been taxed in some jurisdictions, but in others the main revenue from these sources has been through licenses. Following the Bureau of the Census definition, this study would only be concerned with these sources if taxed on some basis related to the income received from the activities.¹³ Licenses themselves, in many cases substantial, can be significant revenue producers. It is question-

¹¹ Municipal Finance Officers Association, *Municipal Nonproperty Taxes*, p. 17.

¹² U.S. Bureau of the Census, *U.S. Census of Governments: 1957*, Vol. III, No. 5, *Compendium of Government Finances*, p. 17.

¹³ U.S. Bureau of the Census, *Compendium of State Government Finances in 1960*, definition of terms, p. 64 and 67.

able, however, that any school district could utilize a licensing power since this is normally related to general government and the protection of the public welfare. Gambling devices or games other than the parimutuel horse race betting, which is normally controlled by the State, are legal in only a few States and are, therefore, of limited potential significance.

Economic Impact

In extending the base or adjusting the rates on activities in the amusement area, there are some basic effects which must be considered. There is always the possibility, by taxing one segment of the amusement industry, that the resultant differential in price may encourage a shift in patronage to another segment. Because of the strong influence of taste and fad in this area, it is probably impossible to get a direct measure of the influence of taxation in these shifts. Since this is an area of flexible demand, it is reasonable to assume that certain activities could almost be taxed out of existence if the rate were high enough. There is no strong indication that rates of 20 percent or higher which have been or are used in many areas have had a serious effect, but any local jurisdiction will have to consider the possible discriminatory effects on the amusement industry in the event of proposing an increase in rate or the establishment of a new rate.

The decline in movie attendance in the postwar period, for example, is usually related to the growth of television rather than the level of taxation. The shift to drive-in movies and suburban location is once again probably more closely related to the modes of transportation and the residential patterns of the postwar period than to downtown taxes.

Regulatory Aspects

Another argument of considerable importance is the attitude toward and the desire to encourage or discourage certain types of recreational activities. This is illustrated by the reluctance to tax participation activities such as bowling,³⁴ swimming, and golf as opposed to the spectator sports which have been traditionally taxed. While there are aspects of recreation in both which could be similarly taxed, the participation sports tend to be favored on the basis of their health building nature. This may

³⁴ The Pennsylvania courts have denied local authority to tax bowling under an "admissions" tax. See Richard F. Schier, *The Legislative and Judicial Development of Act 481: 1947-59*, p. 44-45.

become even more potent with the current emphasis on the state of physical fitness of our youth and society. Unless many of these activities are added to the amusement and admissions tax base, the likelihood of substantially increasing yields is slight, since the major recreational growth has been in these areas.

Unlike the liquor tax or cigarette tax, the amusement tax has rarely been used to discourage activities or been justified on those grounds. To the contrary, legalized gambling has, in the few cases where it exists, been supported by arguments relative to the amount of tax revenue it produces. The possible exception might be the Federal gambling taxes or licenses which are to a large degree designed to apprehend or aid in the prosecution of illegal gambling. Horse racing, like weight pulling contests, may be justified on grounds of "improving the blood," but the revenue producing factors are today significant because of the parimutuel system or betting activities, and the State "take" is never set to discourage participation.

Conclusions

School districts might well find it difficult to tax either health-related or gambling activities, even if legally possible. Without these factors in the base the yield is likely to be small and, for any district other than a large city or suburban area, almost insignificant. As a consequence, even in spite of its particularly fine adaptation to local administration, the admissions and amusement taxes may remain as a small source for local general government but will probably have only limited application to school districts.

Public Utility Taxes

The most widely used local nonproperty tax is one which in a variety of forms falls upon public utilities. The most common form is a tax upon the gross receipts of the utility, but the tax may also be applied to the consumers' utility bill, or levied as a flat rate on some unit of measure associated with the utility such as poles or conduit length, or applied on a per unit basis of the commodity provided such as kilowatts or thermal units. The tax may be in the form of a franchise tax or license fee, but the concern with it here is only to the extent that it is revenue producing and not regulatory.

The tax may cover any or all of the utility services provided

a community; however, a distinction will not be made between the types of utilities as a basis for differentiating the tax. In 1955 some 341 cities over 10,000 population were imposing taxes on public utilities including bus and street railway, taxicab, electricity, gas, refrigeration, steam or heating, telephone, telegraph, and water. The rates of taxes ranged from one-tenth of 1 percent to 14 percent, with an average rate of 2.69 percent. Per capita yields ranged from \$0.02 to \$12.48 and averaged \$2.31.³⁵

The most popular public utility taxes are on gas, electricity, and telephones in that order.³⁶ All public utility taxes at the local level produced \$268 million in 1960.³⁷ This placed public utility taxes second only to general sales taxes as a local non-property revenue source. Included in the local governmental use of this source are a few school districts, mostly in New York State. School districts in cities under 125,000 population in that State are authorized to levy a 3 percent consumers' utility tax. In 1958 this tax imposed by six city districts produced \$1.2 million which on the average equaled about \$1 per thousand dollars of the full valuation of property in those districts.³⁸

A negligible amount of money also accrues to the county school districts in Nevada from the proceeds of a 2 percent net profits tax on utilities outside of incorporated cities. This tax really appears to be a State tax though collected by the counties and returned to the local units. As in the case of other nonproperty taxes, the collections made in dependent school districts can be ignored.

Consumer Incidence

As has been indicated, the public utilities tax can be found in many forms. It can be generally stated that, whatever the initial impact, the incidence of these taxes will be upon the consumer. This results from the regulated monopoly status of these enterprises which allows a rate sufficient to produce a reasonable level of profit. Any tax which is placed on gross receipts will simply result in a rate increase to provide the necessary profit margin. The only real distinction between a tax placed on the consumer directly or the utility itself is in the visibility of the tax. The

³⁵ Municipal Finance Officers Association, *Municipal Nonproperty Taxes*, p. 29, 35, and 37.

³⁶ *Ibid.*, p. 29.

³⁷ U.S. Bureau of the Census, *Governmental Finances in 1960*, table 1, p. 16.

³⁸ Arvid J. Burke, Mabel Walker, and Anne Phinney, "Local Nonproperty Taxes," p. 90 and 93. There are now seven cities using this authority.

consumer utility tax will be separately stated on the bills rendered by the utility, while a tax on gross receipts, for example, will result in increased rates. The taxpayer is more aware of the tax in the former case, and the degree to which the local community wants the tax acknowledged will determine the form.

Administrative Costs

There will be some differences in administrative cost depending on the form of the tax, but in no case is it likely to affect the tax revenues to the local unit. Public utility taxes are extremely easy to administer from the point of view of the local official because they normally involve only a few taxpayer accounts. In New York, for example, Syracuse had a total of 72 taxpayers registered while Elmira had only 9.³⁹ It is the utilities themselves which must bear the major administrative costs though these, too, will ultimately be reflected in higher utility rates. In the case of gross receipts taxes the administrative costs should be almost negligible, and even in the case of consumer taxes the use of modern billing and accounting techniques should keep the costs to very low levels.

The major administrative cost which will face the taxing jurisdiction is the auditing of taxpayer accounts to assure compliance. The city of Miami, Florida, which taxes purchases of electricity, metered gas, bottled gas, and telephone service spent for administration approximately one-fourth of 1 percent of \$1,970,000 collected in fiscal year 1954 from a tax on these sources. While the percentage would vary from jurisdiction to jurisdiction, in no case should the administrative cost be high.⁴⁰

Economic Impact

While it has been stated that the incidence of the public utility tax on the consumer is assured by the monopoly status of these utilities, it should be noted that there may be some competitive aspects between different utilities. For example, residential and commercial heating may be provided by gas, oil, electricity, coal, or steam, to mention the major sources. Air conditioning may be provided by either gas or electricity. Public transportation may be provided by streetcars, subways, buses, or taxicabs and all compete with private automobiles at the local level.⁴¹ Each

³⁹ Frederick D. Stocker, *Nonproperty Taxes as Sources of Local Revenue*, p. 51.

⁴⁰ W. E. Nichols, "Administering a Consumer Utility Tax," p. 157.

⁴¹ Trains and air transportation have only limited applicability at the local level.

of these utilities provides a degree of service for which the demand is inflexible and profits assured for a fixed level of operation in relation to population, but the acquiring of a large market is dependent to a great extent upon taking customers from a different utility. The rate which must be charged, therefore, becomes significant in a market expansion.

Bearing in mind these interrelationships, one should check the taxing of any single utility for possible discriminatory effects. Some utilities such as water and telephone may not have any effective competition though very high rates may reduce consumption or use. Taxation of nonutility companies such as heating oil, bottled gas, or coal distributors may be warranted in order to maintain an economic balance, and several jurisdictions have done this. The extension of these taxes to nonutility energy distributors would add somewhat to administrative costs, but even here the number of such distributors is relatively limited.

Equity Considerations

There may be a problem of equity involved in the choice of the application of a tax on utilities.

Large v. small consumer.—If the tax is a percentage of the selling price of the commodity or service, whether imposed as a gross receipts tax or directly on the consumer's bill, there will be a tendency for the tax to fall heavier on the smaller consumer. This is related to the fact that the price charged per unit of sale or service often declines as quantity of consumption increases. This is compounded by a declining schedule of utility tax rates used in some communities beginning, for example, with a 10 percent rate on bills under \$500 and declining by steps to maybe 1 percent on all bills over \$1,500.

One group has suggested that such a tax be placed on a unit basis, particularly for energy sources, thereby eliminating the discrimination against small consumers and at the same time maintaining an economic balance between competing suppliers of energy, since it is assumed that price differentials embody a consideration of different energy potentials.²² On the other hand, of course, if there are economies reflected in the price for large consumers, this will have to be weighed on the equity balance.

Relation to property taxes.—It is sometimes argued that public utility taxes are closely related to property taxes because of the

²² Financial Advisory Committee for the Montgomery County (Maryland) Council, *Montgomery County Revenue Survey*, January 19, 1960, p. 35-37.

residential nature of many such utility services, and that they therefore do not offer much in the form of property tax relief. While it is true that the same taxpayers are probably involved in both taxes, such is the case of all of the broad based taxes. The public utility taxes are probably the broadest based of all the selective sales taxes, and there are few if any persons that can escape them entirely. There can be no assumption, however, that the taxpayers pay utility taxes in the same proportion that they pay property taxes. While more expensive homes will ordinarily use more utility services, the increase in use is not necessarily proportionate. There is one factor that may pull them fairly close together in some communities and that is the tendency for more expensive homes to be assessed at a lower ratio than medium-valued homes.

Degree of regressivity.—In effect the public utility taxes carry about the same degree of regressivity as the property tax—sometimes less and sometimes more. There are no indications that they are any more regressive than most of the other selective sales taxes which have been discussed, since small degrees of regressivity are virtually impossible to differentiate. For communities that utilize a regressive table of tax rates, of course, the utility tax is likely to become more regressive. If the steps are large in terms of utilities used, then the purpose is probably to exclude large industrial consumers from the full impact of the tax as an incentive or concession to business.

Conclusions

Public utilities taxes can produce substantial sums of money if the rates are made sufficiently high. There are several jurisdictions in Florida and Georgia where the yield of these taxes approach and even exceed the property tax on a per capita basis, although this reflects an unusual situation. In most cases such taxes could only equal a portion of the normal property tax yield, but a substantial portion, if desired.

Since the yield is adequate and the administration is quite simple, the major consideration of any school district in attempting to decide on the use of public utility taxes would be whether the adoption of such taxes would be considered as a sufficient change from the property tax base to afford relief, psychological or otherwise. Even if these taxes do have a close relationship to property, they have the advantage of easy monthly payments which is not generally true of the property tax.

Real Estate Deed Transfer Tax

The real estate deed transfer tax cannot truly be called a non-property tax in that it is levied upon property. Like the property tax it is ad valorem but ordinarily at a fixed percentage of the selling price rather than a percentage of assessed valuation. Unlike the property tax, it applies only to property that changes hands, it is a one-time tax based on each transaction, and it may be applied more than once during the fiscal year if the property changes hands that frequently.

Local units in five States⁴³ tax the transfer of title to real property, and this includes school districts in Pennsylvania.⁴⁴ In the State of Washington only counties may levy this tax and the proceeds must be devoted to education.⁴⁵ In the other three States school districts in local areas using the tax are dependent, though receiving no direct benefit. In most cases the rate charged is 1 percent and this represents the maximum in current use. In a few cases exemptions for property below a certain value are provided.⁴⁶

Justification

There is at least one rationale which can be used to justify the application of these taxes in modified form in most communities. The construction of new homes in a community creates at once a requirement for capital construction of local governmental facilities—water and sewage lines, roads, schools and possible expansion of fire, police, and health and welfare facilities. A real estate transfer tax on new property might be justified on grounds that the one-time tax would make a contribution toward these added capital needs. One committee surveying a growing suburban community estimated that a 2 percent tax on new property would provide annually 53 percent of the current debt service charges or 25 percent of actual capital expenditures, a substantial amount.⁴⁷

Present taxes which apply to all transactions (new or used) or exempt lower valued property, which create most of the capital needs, are obviously not based on this rationale. A counter argument to the rationale itself would be that such capital improve-

⁴³ Maryland, New York (New York City), Pennsylvania, Virginia, and Washington.

⁴⁴ Three hundred forty-seven school districts collected \$5,149,218 from this source in 1967-68.

⁴⁵ Municipal Finance Officers Association, *Municipal Nonproperty Taxes*, p. 22.

⁴⁶ \$20,000 in Montgomery County, Maryland, and \$25,000 in New York City.

⁴⁷ Financial Advisory Committee for the Montgomery County (Maryland) Council, *Montgomery County Revenue Survey*, p. 26.

ments should be met by borrowed funds paid off by all homeowners in the future just as they generally have been in the past.

In some localities there may be another justification for this tax. In the past, at least, there has frequently been a delay of a year or more from time of construction to placing on the tax rolls. A transfer tax on new property might be justified as a pickup device. Modern property tax administration limits this delay and thereby the justification.

The most convincing rationale for these taxes, however, is probably that of expediency. The number of taxpayers affected at any one time is small, those affected are usually newcomers rather than the established citizen with a voice in local affairs, and the administration and enforcement of the tax is extremely simple since the transfer of real property involves a recordation procedure with local governmental officials. Equity arguments, therefore, become of relatively little consequence unless one shifts to a different rationale, such as the capital concept mentioned above.

Conclusions

The use of a real estate transfer tax might be justified by school districts on capital improvement, tax pickup, or expediency ground, but the tax is limited largely to growing suburban districts if the yields are to be significant.

Miscellaneous Taxes

There are a variety of selective sales taxes which might be considered by school districts under special circumstances, but they are not generally of sufficient applicability or popularity to warrant extended consideration in this study. Some resort cities and tourist centers have utilized a tax on hotel rooms to produce fairly substantial revenue. This tax has the advantage of tapping nonresident sources almost exclusively but is not applicable in most jurisdictions and would have extremely limited use by school districts.

Taxes on restaurant meals would have wider applicability at least in urban areas, but it is not confined to nonresident taxpayers; and unless there is a substantial minimum charge exemption, the tax could be highly regressive.

In financial centers, stock transfer taxes may be lucrative, but the number of such centers is limited.

New York City even applied a short-lived tax on cab fares,

but this would provide relatively little revenue in most jurisdictions even if one could overcome the vociferous objections which are likely to ensue.

Taxes on soft drinks would offer potential in most areas and are taxed by six States⁴⁸ but not by any local units so far as is known at the present time. Since consumption of these beverages falls so heavily among children and youth, there is probably considerable reluctance to impose such a tax, though the burden would be largely borne by adults and the tax might even be absorbed by producing companies, depending on the rate of tax and the condition of profits.

Conclusions

As indicated in the introduction to selective sales taxes, there is perhaps no limit to the types of such taxes which could be imposed, other than the limit on the types of commodities and services available in the economy. In general terms most of these taxes are neither substantial in yield nor appropriate for school district financing. Need or special circumstances may dictate the choice of such a tax or taxes, however, and the foregoing discussion has been designed to outline the potentialities and problems of the more extensively used selective sales tax sources.

⁴⁸ Commerce Clearing House, *State Tax Guide*

CHAPTER 9

Application of Nonproperty Taxes to Local School Districts

HAVING EXAMINED in some detail the various nonproperty taxes which might be available for use, one must still determine which taxes should be used by a particular school district. In this final chapter some guidelines will be given toward possible tax adoptions, but it must be reemphasized that there are always peculiar local circumstances which must be taken into account, and these are beyond the scope of any general study.

The pattern of State aid to local schools has a strong effect on the need or desirability of adopting local nonproperty taxes. Since State aid comes almost entirely from nonproperty sources, it is obvious that, when a State provides a relatively high proportion of the total school budget, nonproperty taxes are playing a significant role. There is unfortunately probably no absolute level of State aid which could be used to indicate a desirable proportional relationship between property and nonproperty taxes. Each State and local unit must pass judgment on this level, though it would be safe to assume in most cases, for example, that where the level of State support reaches 80 percent, the property tax at the local level is unlikely to be overburdened. The size of the local budget on a per pupil basis is a modifying factor since a high per pupil expenditure even with high State aid might result in high property taxes. This is unlikely under most State programs, however, since high State aid comes almost exclusively through equalization, and the equalized districts are usually operating at minimal levels.

At the other extreme it may be safe to assume that districts receiving less than 20 percent State aid are facing the problem of an overburdened property tax unless local nonproperty sources are already being used. These districts are likely to be the urban and suburban districts under the typical pattern of State aid.

Even these extreme limits may not be valid indicators, and there are many questions which need to be raised with respect to the districts falling between. Wide variations in wealth per

pupil within States means that a nominal tax rate in one district may produce as much or more than an excessive rate in another. The definition of an excessive property tax rate is almost impossible to develop, at least to the satisfaction of a preponderant majority. Rates exceeding 2 percent of true value will usually bring widespread complaints, but this, too, is dependent to some extent upon the total of other taxes which must be paid.

In many States, for example, the property tax paid by most of the families will represent less than half of the total State and local taxes which they pay. Since property taxes today represent about 45 percent of total State and local taxes as compared with over 80 percent 50 years ago, it is quite obvious that a 2 percent rate now could be considered more of a burden than a 2 percent rate then. The variation in property tax load per capita between States today is also extensive, ranging from 12.6 percent to 70.5 percent of all State and local taxes per capita.¹ While these figures above do not prove the case, they do indicate that a certain percentage rate of the property tax in one State or locality is quite likely to be viewed differently from that same percentage rate in another State or locality.

What is "excessive" is, indeed, primarily a problem in psychology rather than tax facts. No one has yet determined what amount of tax information is required to overcome long prevailing attitudes on tax matters. This is one of the major factors in the local tailoring process for an acceptable tax program.

Whatever criteria are used to determine a desirable level of State aid, it is quite likely that large numbers of school districts will still be faced with the necessity of adjusting their local tax programs. On this assumption the following broad guidelines can be given.

Continuing Role for Property Tax

No local district is likely to consider abandoning the property tax altogether. The role of the property tax is too firmly implanted in the pattern of school finance, and this tax offers some advantages worthy of continuation. Stability of revenue and flexibility of rate are its two most highly claimed virtues. While it is easy to administer from the school district's point of view, since somebody else does it, the administration of the property tax is actually its major drawback. If the assessment practices could be sharply upgraded and provisions made for other than

¹ U.S. Bureau of the Census, *Governmental Finances in 1961*, table 19.

lump sum payment, the property tax would compare favorably with many others in use at the local level. There are some who maintain that, even now, it is not regressive over the broad span of middle income and almost proportional.²

The above "ifs" are so big, however, as to be almost insurmountable, in practice. The techniques and knowledge for sound practice are available, but the political pressures and lack of willingness to put them into effect limit severely the potential usefulness of the property tax. After generations of attempted reform, a substitute is more and more frequently being sought, rather than possible reform.

A danger to the schools in continued reliance on the property tax arises from the fact that school budgets may be starved more from a resistance to increases in the property tax than to increases in educational expenditures *per se*. In other words, education must bear a double burden: justification of its expenditure program and justification of the tax that supports it. Only the former should in reality fall upon the schools.

The property tax has had an understandable historic relationship with education as it has with virtually all local governmental functions. Other local governmental functions, however, have been able to draw to a greater extent from other local revenue sources, e.g., service charges, license fees, and nonproperty taxes, thereby lessening their dependence upon the property tax. So long as the property tax is not overburdened actually or psychologically this shifting of burden may benefit the schools, but once the limit of burden is passed, the schools more than any other function are left in the untenable position of having to defend the property tax as a tax. In spite of the many weaknesses and inequities of the property tax, however, no school district is likely to advocate a shift in tax base until this breaking point is reached.

Administrative Feasibility of a Large Number of Local Nonproperty Taxes

Actually there is no reason, other than historical, why the schools should be tied to the property tax. As a matter of fact, history would tend to support the proposition that the property tax, while appropriate in an agrarian economy, should give way to more adequate measures of wealth in our present-day industrial economy. Income and expenditures measurable in absolute rather

² James N. Morgan, Martin H. David, Wilbur J. Cohen, and Harvey E. Braser, *Income and Welfare in the United States*, p. 292-297.

than fictional or assessed dollars of value are far more satisfactory measures of wealth today.

In spite of a fairly general recognition of these facts, continued reliance on the property tax has been urged on occasion because it is the only tax well suited to local administration. This is, of course, largely a myth. The property tax is no better suited to local administration than most other taxes, and the history of its almost universally poor administration proves this. Proper administration of the property tax under its traditional concepts is in fact tremendously difficult and only rarely, if ever, have sufficient funds and effort been made available to ensure a level of equitable administration. Additional funds for proper administration could result in considerable increases in productivity.

Because of its high visibility and relative immobility, the real property tax should have a number of advantages from an administrative point of view. Most of this is in theory, however, and it may be that the malpractices of the past are insurmountable.

It is interesting to note that there is a wide difference in the concepts of administration applied to the property tax and those applied to most other taxes in this country. The basic difference between the property tax and other taxes in the United States is that the property tax is a governmentally assessed and enforced tax while our income and sales taxes are privately or self-assessed, and enforcement is largely through well developed public attitudes encouraged by a spot check auditing system which is designed to catch at least the most flagrant violators.

While electronic data processing makes possible more extensive checking of returns than was practical in the past, there is a recognition of the role that self-assessment plays in our major tax systems today and a concern lest overemphasis on enforcement might change the reasonably successful pattern of tax payments to date.² In some other countries, for example, the income tax has proven unsuccessful because of a widespread attitude which condones cheating on the returns. Also, under such circumstances, there is usually little interest or pressure for the application of effective legal penalties.

In the case of local income and sales taxes, in their wide variety of forms, the fact that the taxes are self-assessed or privately and automatically collected by business concerns through application to sales or through withholding may mean that the administrative burden relative to a fair payment of the tax is less in

² Address of the Honorable Mortimer M. Caplin, Director of Internal Revenue, to a Luncheon Meeting of the National Capital Area Chapter, American Society for Public Administration on September 19, 1962, in Washington, D.C.

these taxes than in the case of the property tax. In only rare cases would the burden be prohibitive or greater than the property tax, if the knowledge readily available for the administration of these nonproperty taxes is utilized. One advantage of adopting a new tax is the possibility of breaking the ties to administrative antiquities of past generations.

The adoption of some self-assessment practices and the use of electronic data processing might improve the local administration of the property tax, but there can be no assumption that its administration would even then be better adapted to local conditions than nonproperty taxes. There are some who feel that the main salvation of the property tax would be to have the States reenter the field and thereby apply statewide uniformity in assessment practices, though there is serious question that these two propositions would necessarily follow each other. Much of the success in administration of local nonproperty taxes may come from Federal and State experience and possible cooperation in providing auditing information.

An analysis of local nonproperty taxes would tend to show that, whatever other disadvantages they might have, administrative feasibility should not in most instances be a serious deterrent. This would be particularly true if the nonproperty taxes were widely used by school districts and administered by another level of government as in the case of the property tax.

School Need for Broad-Based Taxes

One of the advantages of the property tax has been that it provides a broad base for the governmental functions it supports. There has traditionally been a relationship between income and property, and it is this relationship that has been modified in our modern economy. Since the benefits of public education are so broadly distributed, it is appropriate that public education should be broadly supported.

Broad tax support can be achieved theoretically in one of two ways: (1) Through a broad-based tax such as the income or sales tax, or (2) through a combination of lesser selective taxes which in total touch a very broad group. Of these two devices only the first, or use of broad-based taxes, is practical for school districts. There are several reasons for this.

Schools Not Tax Collectors

School districts do not ordinarily function as tax collecting units in and of themselves. They are users of taxes and will

apply a rate which will in fact be collected by an appropriate agency of the general government with the revenue forwarded to the schools. The schools benefit from this arrangement in that a single tax collecting unit may operate more efficiently in carrying out this activity for several units or functions of government. In fact, the cost of collecting the taxes for schools, in most cases, will not even have to be included in the school rate. This is certainly efficient from the point of view of the school district whether or not it is from the overall view of collection costs, and it *should* be more efficient even from that view.

Designated Taxes for Schools

Even though in most cases school districts do not actually collect the taxes they use, the taxes which go to schools are usually earmarked or labeled and are, therefore, closely related to education in the public mind. Proposed new taxes at the State level have often been justified by educational needs. Sometimes these taxes are in fact earmarked for schools, but occasionally the revenue from such taxes is later diverted to other uses.

Selective sales taxes.—A number of selective sales taxes and even general sales taxes have been earmarked in whole or part for schools even though levied by a municipality or county. The selective sales taxes have frequently been the so-called "sin" taxes on tobacco products and alcoholic beverages. These taxes are often easiest to levy particularly if the revenues produced are going for a good cause. There is some question, however, as to whether education should be tied to a selective sales tax which draws revenue from only a portion of the population. No school district is likely to turn down the revenue from any particular tax because it is tainted, a questionable concept at best, but having public education directly supported by a small variety of special or "nuisance" taxes may have the same limiting effect ultimately as the property tax.

Income and general sales taxes.—The schools would best seek to utilize the general sales tax or a form of income tax and leave the area of selective sales taxes to general government which supports a variety of activities from its general fund. The income tax may have special justification because of the documented relationship between level of education and expected life earnings.⁴ Some of this additional income might be tapped to support the educational system which allows its production with possible mul-

⁴ See Herman P. Miller, "Annual and Lifetime Income in Relation to Education: 1939-1959," p. 962-986; and "Income and Education: Does Education Pay Off?" p. 129-146.

tiplier effects even though there may not be a direct or perfect relationship between the locality where the education is provided and the place where the income is earned.

Other broad-based taxes.—There may be exceptions to this general rule in the case of some taxes which are also broad-based. The poll or per capita tax properly applied is as broad-based as any tax and has some advantage in that it elicits a modicum of direct support from each adult citizen. It, of course, violates any progressive or proportional tenets of taxation and, because of its tie to voting in several States, it becomes less than desirable in the eyes of many.

Public utility taxation is certainly as broad-based as the property tax. It can produce sizable sums from a captive consumer group, though there is no reason other than availability which should dictate support of public education by utility users.

Finally the real estate transfer tax, if justified on a capital investment basis,⁵ might qualify for support of education though there are other capital costs of government which would equally qualify. The possible irregularity of yield might also indicate a desirability for the revenues from this source going to a general fund rather than a school fund.

Education Versus Other Government Functions

The desirability of utilizing only the large yield, broad-based nonproperty taxes, when a shift to nonproperty sources is felt necessary, would probably be recognized by many; but some might argue that this same justification could be used for other governmental functions. In some cases, e.g., police and fire protection and health and welfare, this is undoubtedly true. Education as the largest single user of public funds at the local level can, however, enter a strong claim. The other functions mentioned tend to draw their support from the general funds of the government and are not, therefore, tied to the tax or taxes that make up that fund. The independent status of education and its separate treatment even in so-called "dependent" situations tie it more closely to the particular tax sources which provide its revenue.

Diversification or Supplementation

This study does not propose to argue the merits of "independent" or "dependent" relationships but simply indicates that

⁵ See p. 114 above.

under present circumstances the position of public school organization calls for a special orientation toward the tax programs which support it. If diversification from the traditional property tax support at the local level is felt necessary, then the preferable adoption in the nonproperty tax field would be a broad-based income or general sales tax. If all that is sought is some small scale supplementation from nonproperty sources, then there are a wide variety of possible choices though, even here, it would be preferable to choose from among those with the broadest possible bases.

School government is not general government, and every effort should be made to deemphasize the tax collection function which is not, in fact, a role played by the schools. The separate nature of school finance and the consequent direct relationship to revenue sources makes it advisable to keep these sources as broad as possible in order to simplify this aspect of school administration and allow full concentration on the service role of education.

Relation of Tax Program to Economy of Area

In order to be productive and equitable, a tax program must be related to the economic structure of the community. The economic structure will in turn be closely related to the geography and population of the area.

Wealth Necessary for Taxes

It becomes a truism that no tax program can produce adequate revenue if economic wealth is not present. Some school districts may have so little economic wealth in relation to the population that no local tax program, property or nonproperty, can provide relief. In these cases either the districts must be geographically modified to bring in additional economic wealth or aid from another level of government must be obtained. These are problems which have been long recognized, and various solutions of reorganization and State aid have been applied or recommended.

For the purposes of this study it is assumed that these districts lie outside the scope of consideration. It is, however, extremely important that any school district facing financial problems examine, first of all, the question of whether the economic wealth to provide good schools actually exists in the district. If it does have the wealth, then the question of which taxes to utilize for best tapping this wealth can be tackled. It is this latter question which is the concern of this study.

Since the economic aspects and impact of various nonproperty taxes have been discussed in some detail in previous chapters, no attempt will be made to summarize the generalizations that can be made about the economic relationships at this point. The importance of these relationships must be reemphasized, however.

Examples of Tax Programs and Analysis

Having discussed the various aspects and factors of importance in a variety of nonproperty taxes, one can apply this information to two theoretical examples of school districts. These examples must, admittedly, be somewhat oversimplified though not too unreal.

There is no way to establish a theoretically ideal program removed from the actual situation, and each school district will have variations and special conditions to consider. Dealing with a theoretical situation, however, will give some idea of the factors which may be brought into play in a real situation.

Psychological and political factors which can be extremely critical cannot, of course, be applied to these examples with a high degree of reality because of their wide variability. The handling of these problems is beyond the scope of this discussion, though the importance of such problems is readily recognized.

School District Categories

Depending upon the basis for categorizing, there is a wide variety of different types of school districts which could be analyzed. These would range from the small rural to the large city district. In the last complete *Biennial Survey of Education* published by the U.S. Office of Education for 1954-56, statistics were compiled for five different size city school district groups, three suburban city groups, six county unit groups, and four rural county groups. In each case the gradation between groups in each broad category was total population except for the rural counties where degree of ruralness was the distinguishing characteristic.⁶

While it is true that several nonproperty taxes may be feasible for adoption by rural districts, particularly counties,⁷ it is also

⁶ See U.S. Office of Education, *Statistics of Local School Systems: 1955-56*, chapter 3, Section I, "Cities," by Lester B. Herlihy; Section II, "Suburban Cities," by Joel Williams and Tobia Bressler; Section III, "County Units" by Gerald Kahn; and Section IV, "Rural Counties," by Walter H. Gaumnitz, Emanuel Reiser, and Mary Anne Harvey, all separate volumes and part of the *Biennial Survey of Education in the United States 1954-56*.

⁷ Frederick D. Stocker, *Nonproperty Taxes as Sources of Local Revenue*, p. 72.

true that there is likely to be relatively little pressure for the adoption of such taxes in rural communities. The property tax in these areas is more closely related to income, if reasonably administered, because most of the property is income producing in a business sense. Taxes on cash income or expenditures may not be as good a measure of true wealth as the property tax in these cases. Further, in most instances, these areas usually qualify for a high percentage of State aid and the true property tax rates are relatively low. Little consideration of a shift to nonproperty taxes can be expected until a sizable number of the taxpayers consider the property tax too high.

In the case of the large city school districts there is little question about the administrative feasibility of virtually any of the nonproperty tax sources, but there may be strong competition for such use from other local functions. Here the solution to a balanced tax program for the schools may have been preempted by previous city actions, and the schools, alone, must continue to bear the brunt of protest votes against a rising property tax, unless some other action, such as increased State aid, is taken.

For purposes of illustration, and on the assumption that most pressure for local nonproperty tax use lies in the urban areas, two types of districts which are urban in nature but have several different characteristics are discussed below: (1) A central city school district of 400,000 population and (2) a suburban school district including a population of 90,000. In each case the criteria which are important in making a decision relative to a proper tax program are established, and these data are summarized at the beginning of each illustration.

It should be noted that in neither case is the district poor. The valuations per student in average daily attendance will indicate this fact. In addition, the measures of personal income and retail sales support this proposition. As has been indicated above, an assessment of the availability of wealth at the local level is the first thing which needs to be done, for there is no way to tap nonexistent wealth.

Sources of data.—The type of information presented in both illustrations would in practice be developed from a variety of sources. Local school budgets and financial reports or detailed State school finance reports can provide the information on educational expenditures. Municipal or county budgets and financial reports can supply the detail on noneducational governmental expenditures.

Publications of the Bureau of the Census, both the decennial Census of Population and the quinquennial Census of Govern-

ments, are valuable for information on schools and general government. For larger municipalities, fairly detailed information is published annually by the Bureau.

For current projections and estimates local university bureaus of economic research, educational research, and governmental research frequently have at hand or can develop the needed information.

Private compilations such as *Sales Management Magazine's* annual "Survey of Buying Power" are valuable if they cover the geographical unit being analyzed.

One of the difficulties involved in gathering economic and non-educational governmental data for school districts is that frequently the school district is not coterminous with other governmental jurisdictional lines. It is for these other governmental units that most of the data is collected. Depending upon the particular situation, therefore, considerable interpretation and analysis may be involved in providing needed economic data.

The type of data and information provided in the illustrations would be necessary before a sound decision on a tax program could be reached, though these factors alone are not sufficient for this determination. Other social and political factors may become equally important but are not as susceptible to categorization as the economic factors.

Central City School District

Using the summary data below plus some factors which will be introduced in the following discussion, one might proceed to propose a tax program for this hypothetical central city school district.

Summary Data for Central City School District

Economic description	
Balanced industry	
Employing area	
Moderate growth	
Population	400,000
Average daily attendance (ADA)	62,000
School expenditures	
Current expenditures	\$27,000,000
Per ADA	435
Capital outlay	4,500,000
Debt service	3,500,000

NONPROPERTY TAXATION FOR SCHOOLS

Nonschool expenditures for municipal services available in area

Current expenditures	26,000,000
Capital outlay	6,000,000
Debt service	3,300,000

Revenue

Taxes

Property (total)	40,300,000
Schools	18,600,000
Municipal	10,900,000
County and State	4,000,000
Debt service (school and nonschool)	6,800,000
Selective sales (municipal)	1,300,000
Licenses and other (municipal)	2,600,000
Intergovernmental revenue	13,000,000
Schools	7,800,000
Municipal	5,200,000
Charges and miscellaneous	6,600,000
Schools	600,000
Municipal	6,000,000
Assessed valuation	600,000,000
Ratio of assessment, percent	30

Property tax wealth

	Actual	True
Per capita	\$1,500	\$5,000
Per ADA	9,677	32,257

Property tax rate

Actual	\$6.71/\$100
True rate	2.01/\$100

Property tax rate (detail)

	Actual/\$100	True/\$100
Schools	\$3.68	\$1.10
Municipal	2.36	.71
State and county	.67	.20
Total	\$6.71	\$2.01

State taxes

Income tax	Progressive rates 2% to 8%
Sales tax	2%

Personal income \$950,000,000

Annual retail sales 600,000,000

Property tax rate.—Since local districts normally turn to non-property sources because of concern with the property tax rate, it should be noted that the total true rate^a is just over \$2/\$100 or 2 percent of value. While there are no fully accepted standards as to what the top limit of a property tax should be, true rates

^a True rate is adjusted to take into account the ratio of assessment to true value of the property.

of over \$1.50/\$100 or 1.5 percent may be considered high and those over 2 percent exorbitant unless there are no other State and local taxes imposed, not true in this case.⁹ In terms of wealth measured by income or sales in this community, it might not be unreasonable for the property tax to go higher, but there are certain limiting features which can be reiterated at this time.

Property tax payments are normally made annually or semi-annually and, therefore, are highly visible and appear larger than they should in comparison, for example, with the Federal income tax. Further, the older established groups in the community, who are often active voters, anticipate a coming period of declining retirement income and a fixed high property tax.

In addition the property tax represents a tax on debt rather than wealth to younger home owners and is something which must be borne along with substantial interest payments. It may also be interesting to note that with 30-year home loans, a 2 percent property tax rate may seem very close to the average 3.33 percent capital repayment rate.

Finally, assessment inequities become more noticeable and unbearable as the rates increase, a factor which can be good if it results in improved assessment practices but, as is more likely, a limiting factor on further rate increases in the absence of improvement.

The use of fractional assessments which result in high actual rates may also have some negative effect even though it should only be the tax bill which impresses the taxpayer. Fractional assessments may have a very real effect because of statutory or constitutional limitations which either place an absolute ceiling on the tax or force additional levies to a vote.

While the school district levy in this case is only slightly over 1 percent of true value, \$1.10/\$100, it is the total levy that counts since all are combined in a single tax bill. Whatever the reasons, pressure has built up for relief of the property tax, and this community is looking to new sources. It might be either the municipality or the school district, conterminous in this illustration, which would seek additional nonproperty revenue. The schools for purposes of illustration in this case have been faced with competition from the suburbs and need additional salary money and provisions for special classes to meet the needs of a changing urban population and are, therefore, making the initial move.

⁹The reader needs to be warned again of the psychological aspects of the property tax and the wide range of rates which may be accepted in different parts of the country.

Nonproperty tax use by other governmental units.—The State in this illustration is using both major sources of nonproperty taxes—sales and income—so there is no natural drawing of attention to one or the other. The municipality is already using a public utilities gross receipts tax as well as an admissions tax and a deed transfer tax.

Wage tax.—Serious consideration was given to a wage tax, particularly if it would tap nonresidents who work in the city as well as residents. Since the State income tax already ran somewhat higher than average and since it was determined that the State legislature, which would have to authorize the tax, would be hostile to a nonresident tax, if not to the whole wage tax idea, attention was turned to other sources.

Sales tax.—Turning to a sales tax it was noted that the State rate in this case was below average with 23 States having higher rates and no States with regular sales taxes having lower rates. It was estimated that a 1-percent local sales tax would produce approximately \$5,000,000 annually, using the same base as the State tax, which excludes food. It was further proposed that the possibility of State administration of the tax be investigated with a surcharge of 1 percent being added in and for the school district. As a selling point for the tax, it was suggested that one-half of the yield or \$2,500,000 go for property tax relief and the other half for additional school needs. The tax relief involved would amount to approximately 6 percent or a reduction of \$0.42/\$100 in the actual rate.

There was some concern that a sales tax might hurt the city's retail trade, but it was felt that the 1-percent differential would not be significant. An exemption for out-of-district deliveries was proposed, but since it would complicate State collection arrangements it was decided to postpone such an exemption. If later hardship did warrant such action, changes would be considered. In the event that State administration could not be obtained, then separate exemptions could be made, though uniformity between the State and local tax was considered important.

Alternative taxes.—As an alternative to the 1-percent general sales tax, it was estimated that a 4-percent consumer's utility tax on coal, electricity, gas, oil, and telephone and a 3 cents per pack tax on cigarettes would produce slightly over \$2,000,000, which would supply the immediate school needs but provide no actual reduction in the property tax rate. Since the State operated the retail liquor stores, only beer and light wines were eligible to be considered for local taxation. It was estimated that a tax

on beer equivalent to 1 cent for each 12 ounces would produce approximately \$400,000. The use of a poll tax was briefly considered and rejected. If all three taxes—utilities, cigarettes, and beer—were used, some property tax reduction could be achieved.

Conclusions.—While the general sales tax had some drawbacks, it was considered as preferable to a series of selective sales taxes where arguments about the taxes might divert attention from the educational needs. The fact that most of the tax burden would fall upon the district residents was considered as a favorable political factor from the point of view of the State legislature, though some contributions could be expected from sales to commuters and nonresidents. The possibility of State administration and the avoidance of creating a new or larger local administrative agency was encouraging. Finally, there was some feeling that residents of the district might prefer a rise in the rate of a nonproperty tax with which they were familiar rather than experimentation with a new and unknown tax.

Suburban School District

The second illustration of a school district is somewhat typical of many throughout the country. It is located outside the central city with the bulk of its working residents employed in the city. There are several shopping centers and some service industry, but the bulk of property consists of single family residential property. Expenditures for schools dominate governmental costs in the area. While the capital outlay is substantial, the real cost is postponed through the use of borrowed funds and the debt service costs are currently relatively low. The use of relatively high salary schedules to attract new teachers into the growing community has resulted in above average per pupil costs for the State, but these are held down somewhat by the fact that most of the teachers are in the early steps on the salary schedule.

Summary Data for Suburban School District

Economic description

Predominately residential community

Commuting population

Rapid growth

Population -----90,000

Average daily attendance (ADA) -----18,000

School expenditures		
Current expenditures	-----	\$7,500,000
Per ADA	-----	417
Capital outlay	-----	3,200,000
Debt service	-----	600,000
Nonschool expenditures for municipal services available in area		
Current expenditures	-----	4,000,000
Capital outlay	-----	1,000,000
Debt service	-----	200,000
Revenue		
Taxes		
Property (total)	-----	6,650,000
Schools	-----	4,350,000
Municipal	-----	900,000
County and State	-----	600,000
Debt service	-----	800,000
Selective sales (municipal)	-----	250,000
Licenses and others (municipal)	-----	500,000
Intergovernmental revenue	-----	4,200,000
Schools	-----	3,000,000
Municipal	-----	1,200,000
Charges and miscellaneous	-----	1,300,000
Schools	-----	150,000
Municipal	-----	1,150,000
Assessed Valuation	-----	145,000,000
Ratio of assessment, percent	-----	40
Property tax wealth		
	Actual	True
Per capita	-----	\$1,611 \$4,028
Per ADA	-----	8,056 20,140
Property tax rate		
Actual	-----	\$4.58/\$100
True rate	-----	1.83/\$100
Property tax rate (detail)		
	Actual	True
Schools	-----	\$3.41 \$1.36
Municipal	-----	.76 .30
State and county	-----	.41 .17
Total	-----	\$4.58 \$1.83
State taxes		
Income tax	-----	None
Sales tax	-----	3%
Personal income	-----	\$300,000,000
Annual retail sales	-----	100,000,000

Property tax.—State and Federal aid to the schools is more substantial than in the first illustration, running about 40 percent of current cost for this school district. All of the local funds for

schools are derived from the property tax, however, and the current true rate for schools is \$1.36/\$100 or 1.36 percent. Added to this is \$0.47/\$100 true rate for municipal, State, and county taxes which brings the total to \$1.83/\$100 or 1.83 percent. The property tax rate is not increasing rapidly because of the growth in assessable base, but it has already reached the point of protest and promises to go higher. While no reduction in the property tax rate is expected, efforts are being made to find nonproperty sources to meet future needs and avoid an increase in the property tax rate.

Income tax.—A quick examination of the economic data for this school district reveals that the real basis of wealth is personal income. As a consequence, major consideration was given to the use of a local income tax. This was considered particularly appropriate since the State was not utilizing an income tax. In addition to a 3-percent sales tax, the State did levy substantial taxes on gasoline, motor vehicles, alcoholic beverages, and cigarettes and tobacco products which discouraged consideration of local taxes on these particular products.

Potential revenue from a 1-percent flat rate local income tax was estimated at \$2,500,000. This estimate took into account the cost of local administration. Since the proceeds of a 1-percent tax was in excess of the immediate needs unless a substantial reduction in the property tax were planned, a 0.5-percent rate which would produce approximately \$1,200,000 was considered more appropriate. The proportionately smaller estimate for the 0.5-percent rate is based on the fact that the administrative costs would remain the same for the lesser amount. Even this amount would allow some reduction in the schools' portion of the property tax rate. The overall impact on the total property tax rate would depend upon the municipal, State, and county needs.

Objections were raised that such a tax might discourage movement into the district by the more well-to-do families. This was countered by the arguments that the attractions of suburban living could overcome the tax objection and that the same amount of money raised through the property tax would certainly not be more appealing to these groups. In addition it was noted that the central city had been considering a local income tax and that it might be well to establish residence as a basis for such taxes rather than place of work.

The fact that at least one other local jurisdiction was considering the tax opened the possibility that it might be levied on a metropolitanwide basis in the future, an acceptable alternative

with some savings in administrative costs and a lessening of competitive factors so long as it was based on residence.

Alternative taxes.—While the local income tax seemed to offer the best potential, some other alternatives were considered. A 1-percent general sales tax would supply approximately \$700,000, sufficient for immediate school needs, and might offer some advantages through State administration if it could be arranged. The fact that the State collections were not broken down by school districts would involve some extra effort and cost on the part of the State if it did administer a local added sales tax. While most local retail businesses were located on the basis of convenience, it was felt that there might be some competitive disadvantages unless the tax were levied metropolitan areawide. The sales tax did not seem to offer the same growth potential in this case that the local income tax promised.

A consumer's utility tax was estimated to produce about \$500,000 at a rate of 4 percent on telephones, gas, electricity, oil, and coal. Since this district is a growing community with a large amount of residential building, a real estate transfer tax was also proposed as a contribution to the added cost of schools resulting from such growth. A 1-percent tax on the transfer of real property was estimated to yield another \$500,000 per year.

Conclusions.—This school district has several possibilities for nonproperty tax revenue, though the last item, a real estate transfer tax, is closely related to property. It is possible through the adjustment of rates and combining taxes to come up with varying amounts of revenue to meet school needs. The local income tax would offer the greatest potential and flexibility, but in the event it cannot be adopted, there are some other alternatives which will supply substantial amounts.

Additional Factors Affecting Selection

In the brief examination of potential sources for two types of school districts, one is unable to analyze many of the factors which can modify or block attempts to adopt nonproperty tax programs.

Constitutional or statutory limitations.—There may be constitutional or statutory limitations which preclude the adoption of certain taxes. These limitations may be removed, particularly the statutory type, but such removal always involves extensive campaigning and support.

Relationships with the State legislature.—The relationships

with the State legislature may be critical. Opposition to local programs may develop in the State legislature because they affect future State action or because they set precedents which some members of the legislature may not want to see extended to their own area. When one school district is authorized to use a new source of revenue, it is hard to deny that use to other school districts.

Business, labor, and government.—The opposition or support of local business, labor, and civic groups is in most cases extremely important, and these groups may be at odds with respect to different taxes. Able public relations and consultation with these groups can be vital. Other local units of government may also be interested in the tax proposals, and relationships with these units may be important to the adoption of a desired program.

Referendum.—Finally, in many cases the adoption of non-property taxes may involve the referendum or vote by the electorate. In these cases, the selling job or explanation of the tax program to the public may be more important than any other phase of the process. Careful planning and research in the development of the soundest tax program possible for the school district concerned will, of course, make the selling job easier, but rarely will such a program sell itself. Psychological and sociological factors play an important role. Impressions and prejudices may often be more important than logic in the attitudes toward taxes or tax programs. Overcoming these impressions and prejudices can be a tremendous task and may only be achieved in some cases by the occurrence of a crisis, which is usually undesirable from a sound planning point of view.

Conclusions

Local nonproperty taxation for schools has not been widely adopted even though it has been widely discussed. There are several explanations for this limited use. The property tax has until fairly recently provided adequate local revenue in most cases where there was sufficient wealth to meet local needs. Where this wealth did not exist, it was necessary to look to other levels of government which could draw on a broader tax base. In the case of schools this has been predominately at the State level.

The States have withdrawn from the property tax field and this withdrawal has provided more leeway at the local level, at least until governmental service demands increased sharply. It

is generally assumed that the larger units of government can best administer nonproperty taxes and the States have moved extensively into the fields of income, general sales, and selective sales taxation. The Federal Government has long dominated the income tax field and is also heavily involved in selective sales and excise taxation.

At the local level the major adoptions of nonproperty taxes have been made by the municipalities with the net result that the school districts are left in the residual position of being the major users of the property tax and, in turn, dependent almost entirely upon the property tax for their local sources of revenue.

So long as abandonments by other units of government have provided additional potential revenue from this source, or so long as the States have provided additional sums of money from State sources, the fiscal needs of the schools could be met. In more and more cases today, however, the property tax has reached its limit, either constitutional, legal, practical, or emotional. Additional State appropriations have not been forthcoming, and the local district is faced with the direct problem of seeking additional sources of revenue.

This study has attempted to analyze some of the alternatives available in the nonproperty tax field to see how they might be adapted to local school district use. Many nonproperty taxes are administratively feasible for use by local school districts, though they may not always be suitable for other reasons. The property tax is no better suited to efficient local administration than are most of the nonproperty taxes and not as well suited as several. The main advantage that the property tax holds is that it is in existence and being administered at the local level in spite of many inefficiencies. Resistance to change and fear of the unknown are always strong factors.

While an attempt has been made to dispel some of the misconceptions and fears of nonproperty tax use at the local school district level, this study does not necessarily recommend the use of nonproperty taxes, as such. From the point of view of adequate educational financing, there may be several alternatives which are more desirable. There are certain economies in the administration of taxes by a larger unit of government as well as the tapping of a broader base of wealth. Increased State aid, therefore, is held out by many as a most desirable alternative. Some support Federal aid on similar grounds.

Improvement of property tax administration is offered by others as a way to obtain larger revenues on a fairer basis at

the local level. This is a hope, however, which has been held out for generations, and does not appear much closer to fruition today than 50 years ago.

Reorganization of school districts into larger and more efficient units has had strong support in recent years with substantial results.

All of these methods are useful and desirable. When, however, these alternatives are not being utilized and when the school district is being handicapped in its function of providing adequate education for its children, those responsible for the district's operation have a right and duty to examine other possibilities. If resistance to the property tax has reached the point where school budgets are endangered and if for political reasons the school district must rely on its own resources, then it may well turn to one or more of the nonproperty sources discussed herein.

The broadest based taxes should be used where possible, specifically the income and general sales tax, but conditions may not always allow this. The discussion of a broad range of nonproperty taxes is designed to provide information to those school districts which are seeking some guidance. Nonproperty taxation for school districts cannot solve the major problems of educational finance, but it may alleviate the particular problems faced by many school districts in the never ending struggle for adequate revenue.

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